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Article 1

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REAL ESTATE SALES AND THE NEW IMPLIED WARRANTY OF LAWFUL USE

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Real estate parcels are often subject to zoning ordinances, building codes, occupancy rules, restrictive covenants and servitudes, and other limitations on the owner's rights to use the property.[1] These various land use restraints, alone or in combination, can considerably restrict the uses of particular land parcels. The enforcement of land use restraints, however, is often haphazard. Municipalities usually do not check a property for ordinance and code violations unless someone files a complaint or requests an inspection.[2] Private beneficiaries under covenants, servitudes, and easements often forgo enforcement of their rights, whether out of ignorance of their rights, ignorance of violations, insufficient economic motivation, or some desire to maintain good relations with the violating landowners. With enforcement so inconsistent, land use violations can for years remain uncorrected and even undetected.

As a consequence of inconsistent enforcement, landowners often attempt to sell real estate that violates applicable land use restraints. Material violations will be of considerable interest to prospective buyers, especially if the buyer intends to continue the seller's land use practices. Yet, a prospective buyer is unlikely to learn of existing violations unless he makes appropriate inquiries or seeks contractual assurances from the seller that existing uses comply with applicable restraints. The caveat emptor doctrine, despite strong recent criticism,[3] remains the rule governing unlawful land

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1 *See, e.g.*, D. HAGMAN, URBAN PLANNING AND LAND DEVELOPMENT CONTROL LAW §§ 54-89, 152-157, 163-172 (1971) (discussing zoning, building, and housing codes and private restrictions).

2 *See id.* §§ 156-57; C. FIELD & S. RIVKIN, THE BUILDING CODE BURDEN 45-56 (1975) (considering structural and financial problems in building code compliance offices that limit enforcement efficiency).

3 For a recent judicial discussion of conflicting views on caveat emptor in the context of real estate sales, see Cousineau v. Walker, 613 P.2d 608, 614-16 (Alaska 1980).

usages: the buyer has the responsibility for determining whether existing land uses are unlawful by inspecting the property, reviewing municipal ordinances, and checking the seller's title.[4] In most states the seller is not obliged to disclose violations, however material or latent, and makes no implied warranties or representations that the buyer may lawfully continue existing land use practices.[5] For the unsuspecting buyer, the consequences of caveat emptor can be severe.[6]

Common law doctrines long have offered some relief to unsuspecting buyers of real estate not conforming to land use restraints. That relief, however, has been limited in scope, and courts have often denied relief to many buyers with severely disappointed expectations. For example, express representations of lawful use by

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Some courts still cite the doctrine favorably. *See, e.g.*, Oates v. JAG, Inc., 66 N.C. App. 244, 248, 311 S.E.2d 369, 371 (1984) (" 'Although the doctrine of *caveat emptor,* so far as personal property is concerned, is very nearly abolished, it still remains as a viable doctrine in full force in the law of real estate.' ") (quoting Levy v. Young Constr. Co., 46 N.J. Super. 293, 296, 134 A.2d 717, 719 (App. Div. 1957), *aff'd,* 26 N.J. 330, 139 A.2d 738 (1958)), *rev'd,* 333 S.E.2d 222 (N.C. 1985). The best current discussion of the doctrine as applied to real estate sales is M. FRIEDMAN, CONTRACTS AND CONVEYANCES OF REAL PROPERTY § 1.2(n) (4th ed. 1984).

For a historical review of the development of caveat emptor, see Hamilton, *The Ancient Maxim of Caveat Emptor,* 40 YALE L.J. 1133 (1931). Numerous commentators have questioned the doctrine of caveat emptor; many commentators writing recently have focused on the implied warranty of habitability. Four of the best works are Bearman, *Caveat Emptor in Sales of Realty—Recent Assaults Upon the Rule,* 14 VAND. L. REV. 541 (1961); Haskell, *The Case for an Implied Warranty of Quality in Sales of Real Property,* 53 GEO. L.J. 633 (1965); Keeton, *Rights of Disappointed Purchasers,* 32 TEX. L. REV. 1 (1953); and Seavey, *Caveat Emptor as of 1960,* 38 TEX. L. REV. 439 (1960). A good recent survey of the gradual, continuing decline of caveat emptor in real property law is Note, *When the Walls Come Tumbling Down—Theories of Recovery for Defective Housing,* 56 ST. JOHN'S L. REV. 670, 682-93 (1982).

4 *See infra* notes 42-85 and accompanying text.

5 *See, e.g.*, Denton v. Hood, 122 Ill. App. 3d 813, 461 N.E.2d 1069 (1984) (affirming judgment for seller of real estate because record failed to disclose any express representations concerning legality of possible land uses or any intentional concealment of existing violations); *see infra* notes 59-65 and accompanying text (discussing judicial broadening of concept of misrepresentation) and notes 93-102 and accompanying text (presenting cases imposing affirmative duties on sellers to disclose violations).

6 Three recent decisions illustrate the harsh effects of caveat emptor in Illinois, a jurisdiction that follows the doctrine with some rigor. City of Aurora v. Green, 126 Ill. App. 3d 684, 467 N.E.2d 610 (1984) (buyer of five unit apartment building expressly described by seller as complying with zoning ordinances has no recourse when zoning ordinance limits building to two units); Denton v. Hood, 122 Ill. App. 3d 813, 461 N.E.2d 1069 (1984) (no recourse for buyer of property with garage that seller knows is in violation of zoning ordinance); O'Brien v. Noble, 106 Ill. App. 3d 126, 435 N.E.2d 554 (1982) (no recourse for buyer of five acre lot sold as site for construction of home when zoning prohibits all construction). *See also* Lenzi v. Morkin, 103 Ill. 2d 290, 292, 469 N.E.2d 178, 179 (1984) (seller has no duty to disclose to buyer large increase in assessed value of property). *Compare* Kinsey v. Scott, 124 Ill. App. 3d 329, 463 N.E.2d 1359 (1984) (buyer able to recover in misrepresentation after purchasing apartment building with one unit constrncted in violation of building code).

sellers have sometimes resulted in liability for misrepresentation. Yet, courts have often denied misrepresentation relief, typically on the ground that the representation is one of law and therefore not a proper subject for a misrepresentation action,[7] or on the ground that the buyer should have detected the seller's misrepresentation through a diligent inspection of public records.[8] Sympathetic courts have occasionally granted rescission or restitution based on mutual mistake or unjust enrichment, but many courts consider the risk of illegal use foreseeable and place that risk on the buyer.[9] Buyers can most readily obtain relief if the illegal use renders the seller's title unmarketable. Many illegalities, however, do not affect title marketability,[10] and relief for unmarketable title is available only if the illegal use is identified before the sale closes and if the seller has not followed the common practice of contractually limiting his obliga-

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7 *See infra* notes 27-41 and accompanying text.

8 *See infra* notes 42-58 and accompanying text.

9 *E.g.*, Luciani v. Bestor, 106 Ill. App. 3d 878, 882, 436 N.E.2d 251, 255 (1982) (no rescission where status quo ante cannot be restored); Lawton v. Dracousis, 14 Mass. App. 164, 172-73, 437 N.E.2d 543, 548 (1982) (purchaser assumed risk of mistake concerning building code volations); Lenawee County Bd. of Health v. Messerly, 417 Mich. 17, 32, 331 N.W.2d 203, 210-11 (1982) (contract clause providing that buyers agreed to accept property "in its present condition" operated to allocate risk of loss to buyers); DiDonato v. Reliance Standard Life Ins. Co., 433 Pa. 221, 224, 249 A.2d 327, 329 (1969) (purchaser of real estate bears risk of zoning ordinance changes occurring after execution of sales agreement but prior to conveyance). *See infra* notes 113-17 and accompanying text.

10 *See* M. FRIEDMAN, *supra* note 3, §§ 3.5 to 3.8; R. CUNNINGHAM, W. STOEBUCK & D. WHITMAN, THE LAW OF PROPERTY § 10.12, at 686-94 (1984) [hereinafter cited as THE LAW OF PROPERTY]. As a general rule, violations of building codes and housing occupancy rules do not render title unmarketable. M. FRIEDMAN, *supra* note 3, § 3.6, at 246-51; THE LAW OF PROPERTY, *supra*, § 10.12, at 694. Courts are split as to whether zoning ordinance violations render title unmarketable, with perhaps a majority now concluding that they do, at least if the violation is material and if it arises from a structure on the land rather than some use of the land. M. FRIEDMAN, *supra* note 3, § 3.8, at 260-65; THE LAW OF PROPERTY, *supra*, § 10.12, at 694; Annot., 39 A.L.R.3d 362 (1971). *See, e.g.*, Staley v. Stephens, 404 N.E.2d 633, 636 (Ind. Ct. App. 1980) (violation of building lot setback requirement renders title unmarketable); Marathon Builders, Inc. v. Polinger, 263 Md. 410, 418, 283 A.2d 617, 622 (1971) (zoning density requirement that prohibits all construction is not encumbrance). Covenants and easements are encumbrances that will almost always render title unmarketable, even if not violated, unless the buyer has expressly or implicitly agreed to take the property subject to them. *See* M. FRIEDMAN *supra* note 3, §§ 4.9, 4.13(d); THE LAW OF PROPERTY, *supra*, § 10.12, at 693. A restrictive covenant renders title unmarketable even though it substantially duplicates a particular zoning or building use restraint which itself does not affect marketability. *See, e.g.*, Coons v. Carstensen, 15 Mass. App. 431, 446 N.E.2d 114 (1983). Recent decisions provide some indication that courts are beginning to relax marketable title rules to increase title marketability when a defect does not actually affect the use and enjoyment of a parcel. *See, e.g.*, Mucci v. Brockton Bocce Club, Inc., 19 Mass. App. 155, 159, 472 N.E.2d 966, 969 (1985) (minor encroachment of structure off property does not render title unmarketable because encroachment would not cause prudent person to hesitate before investing).

tion to convey marketable title.[11]

This Article considers the remedies available to buyers of property that is used contrary to land use restraints. It first examines the growing tendency of courts to broaden the liability of sellers for misrepresentation by weakening or eliminating elements of the misrepresentation action and by construing various actions of sellers as implied, actionable representations that current land uses are lawful. These changes in the longstanding elements of misrepresentation law, it is asserted, are appropriate in this particular setting because traditional misrepresentation law poorly reconciles the conflicting interests of buyers and sellers. This Article also discusses the availability of rescission and restitution for disappointed buyers and the increasing tendency of courts to require sellers and brokers to disclose land use violations and other matters materially affecting the value of the property.

These erosions of the caveat emptor doctrine reflect a growing judicial willingness to protect real estate purchasers who assume they can continue existing land uses and can rely on seller assertions that particular land uses are permissible. Tort-based theories of recovery, however, are ill-suited to provide full relief for buyers and fail to accommodate fairly the conflicting interests of real estate buyers and sellers. An approach that better accommodates these conflicting interests—an approach that courts may soon employ as they further increase protections for buyers—is the creation of a new lawful use warranty that would be implied in all real estate contracts. Under this approach, a seller would implicitly warrant that existing uses of a parcel and any other uses described by the seller comply with applicable land use restraints. This Article discusses the benefits of this new implied warranty and considers the major issues that a court or legislature will face in developing and refining it.

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11 The seller's obligation to convey marketable title lasts only until deed delivery; thereafter, as a result of the doctrine of merger, the buyer must rely for relief on title covenants, if any. M. FRIEDMAN, *supra* note 3, § 7.2, at 781-84; THE LAW OF PROPERTY, *supra* note 10, § 10.12, at 695-98. Sellers commonly limit their obligation to convey marketable title by contract clauses that obligate the purchaser to accept title subject to specified or generally described restrictions and encumbrances. *See* M. FRIEDMAN, *supra* note 3, §§ 3.6 to 3.7, at 251-60, § 4.13(d), at 539-44, § 4.13(b)(3). As a general rule, such clauses do not cover violations of land use restraints, and buyers can still complain of unmarketable title even if they have agreed to such clauses. *See, e.g.*, Madhavan v. Sucher, 105 Mich. App. 284, 306 N.W.2d 481 (1981); M. FRIEDMAN, *supra* note 3, § 4.13(d), at 541-43; THE LAW OF PROPERTY, *supra* note 10, § 10.12, at 690. If the buyer accepts the deed without knowledge of a land use illegality, he can sue only on title covenants. Violations of building, housing, or similar municipal codes do not violate title covenants; courts have only occasionally viewed zoning violations as encumbrances under covenants against encumbrances. *See, e.g*, Monti v. Tangora, 99 Ill. App. 3d 575, 581-82, 425 N.E.2d 597, 602-03 (1981) (building code violation not encumbrance); THE LAW OF PROPERTY, *supra* note 10, § 11.13, at 813.

A new implied warranty of lawful use, similar in operation to warranties of title[12] and the implied warranty of habitability,[13] would markedly improve upon existing tort-based approaches to the problem of land use illegalities. The implied warranty of lawful use would better protect the legitimate expectations of buyers, would greatly simplify the factual disputes in litigation, and would provide greater commercial certainty and flexibility for sellers by defining more precisely their responsibilities to buyers. Moreover, the implied warranty would restore contract law as the framework of seller-buyer dispute resolution. This restoration seems desirable, for contract law better resolves disagreements between buyers and sellers concerning the characteristics and qualities of property than does tort law.

Before considering this new implied warranty, this Article examines in detail the ongoing transformation of misrepresentation law. In the course of this examination, the Article considers some of the realities of the real estate market and explains why sellers should be obligated, whether in tort or in contract, to warrant absolutely that existing land uses are lawful except as otherwise disclosed.

I

MISSTATEMENTS OF LAWFUL USE AND THE ONGOING TRANSFORMATION OF MISREPRESENTATION LAW

Sellers misstating the legality of an existing or proposed use of their real estate traditionally have enjoyed immunity from liability for their assertions. Express oral statements by sellers did not constitute contract warranties because of the parol evidence rule,[14] the statute of frauds, and the doctrine of merger.[15] Such seller state-

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12 On covenants of title in deeds, see THE LAW OF PROPERTY, *supra* note 10, § 11.13.

13 For discussions of the recently developed warranty of habitability, see Haskell, *supra* note 3; Knappenberger, *Extension of Implied Warranties to Developer-Vendors of Completed New Homes,* 11 URB. L. ANN. 257 (1976); Mallor, *Extension of the Implied Warranty of Habitability to Purchasers of Used Homes,* 20 AM. BUS. L.J. 361 (1982); Shedd, *The Implied Warranty of Habitability: New Implications, New Applications,* 8 REAL EST. L.J. 291 (1980); Note, *Implied Warranties in New Home Sales—Is the Seller Defenseless?,* 35 S.C.L. REV. 469 (1984).

14 Professor Corbin provides the following definition of the parol evidence rule:

> When two parties have made a contract and have expressed it in a writing to which they have both assented as the complete and accurate integration of that contract, evidence, whether parol or otherwise, of antecedent understandings and negotiations will not be admitted for the purpose of varying or contradicting the writing.

3 A. CORBIN, CORBIN ON CONTRACTS § 573 (1963).

15 The statute of frauds and the doctrine of merger (by which all of the seller's obligations are merged into the deed and cannot serve as a basis for liability imposed on the seller when the deed has been delivered) also restrict the creation of warranties. *See* D. WHALEY, WARRANTIES AND THE PRACTITIONER 228-35 (1981); Metzger, *The Parol Evidence Rule: Promissory Estoppel's Next Conquest,* 36 VAND. L. REV. 1383, 1391-1403 (1983);

ments also failed to give rise to tort liability under the established elements of misrepresentation law. Misrepresentation liability traditionally arose only if the injured plaintiff could show: (1) a false statement of fact by the defendant, (2) the defendant's knowledge that the statement was false (or some equivalent scienter), (3) an intent to induce reliance by the plaintiff, and (4) actual, justifiable reliance causing damage to the plaintiff.[16] When rigorously applied, these traditional misrepresentation elements operated to deny recovery to nearly all injured buyers.

Deceived buyers seeking relief in misrepresentation have long faced a particularly difficult hurdle in proving the existence of a false statement of fact, particularly in states that adhere to the requirement in its original, technical form. Courts applying the requirement distinguish statements of law from statements of fact and impose liability for misrepresentation on sellers only for factual misstatements.[17] For example, assertions about the zoning status of property,[18] the permissibility of some existing or proposed use under a zoning ordinance,[19] a building's compliance with building codes,[20] the consistency of some specified use with a local development standard,[21] and the need to obtain a permit before engaging in a particular activity[22] have all been viewed by courts as opinions of law that cannot give rise to tort liability, no matter how express and how effective in inducing detrimental reliance.

Bearman, *supra* note 3, at 548-50; Note, *supra* note 3, at 682-87. Although these commentators indicate that the limitations on oral warranties are regularly criticized, the limitations remain alive in some jurisdictions. *See, e.g.*, Reimer v. Leshtz, 90 Ill. App. 3d 980, 982-83, 414 N.E.2d 114, 115-16 (1980) (discussing doctrine of merger and parol evidence rule) (dictum); Rouse v. Brooks, 66 Ill. App. 3d 107, 111, 383 N.E.2d 666, 668-69 (1978) (in contract action, parol evidence rule barred claim for breach of oral warranty of quality in real estate sale absent allegations of fraud or mistake).

16 PROSSER AND KEETON ON THE LAW OF TORTS § 105, at 728 (W.P. Keeton 5th ed. 1984) [hereinafter cited as PROSSER AND KEETON ON TORTS]. Some courts discuss justifiable reliance and actual damage as separate elements in a cause of action for fraudulent misrepresentation. *See, e.g.*, Soules v. General Motors Corp., 79 Ill. 2d 282, 286, 402 N.E.2d 599, 601 (1980).

17 *E.g.*, Northernaire Prods., Inc. v. County of Crow Wing, 309 Minn. 386, 389, 244 N.W.2d 279, 281-82 (1976) (misrepresentations of law only actionable if defendant, learned in field, took advantage of the "solicited" confidence of plaintiff or if defendant and plaintiff stand in fiduciary relationship). *See* PROSSER AND KEETON ON TORTS, *supra* note 16, § 109, at 758-59; Cavico, *Fraudulent Misrepresentation of Law—Are the Exceptions Swallowing the General Rule?*, 11 N. KY. L. REV. 19, 19-23 (1984); James & Gray, *Misrepresentation—Part II*, 37 MD. L. REV. 488, 494 (1978).

18 Davis v. Northside Realty Assocs., Inc., 165 Ga. App. 96, 299 S.E.2d 186 (1983).

19 City of Aurora v. Green, 126 Ill. App. 3d 684, 467 N.E.2d 610 (1984); Gatz v. Frank M. Langenfeld & Sons Constr., Inc., 356 N.W.2d 716 (Minn. 1984).

20 Scott v. Wilson, 15 Ill. App. 2d 456, 146 N.E.2d 297 (1958).

21 O'Brien v. Noble, 106 Ill. App. 3d 126, 435 N.E.2d 554 (1982).

22 Northernaire Prods., Inc. v. County of Crow Wing, 309 Minn. 386, 244 N.W.2d 279 (1976).

Actions by buyers not floundering on the law-fact distinction have often failed because a buyer's reliance on a seller's statement of lawful use is considered unjustified by many courts when the buyer through diligent action could have determined the statement's truth.[23] Thus, a buyer in many states cannot rely on a representation of zoning status or housing occupancy code compliance but must instead independently check municipal ordinances and determine a land parcel's compliance through an actual physical inspection.[24] Other buyer misrepresentation claims have failed because of insufficient evidence that the misstating seller knew of the illegal use or otherwise acted with the requisite scienter,[25] and because the buyer failed to prove that the seller's misrepresentation influenced his conduct directly and definitely enough to satisfy the requirement of actual reliance.[26]

Recently, courts in many jurisdictions have reassessed the merits of caveat emptor and have undertaken to provide substantially greater relief to injured buyers. Courts have granted this relief, not by altering traditional limits on contract-based recovery, but rather by radically reducing or eliminating most of the traditional hurdles for recovery under a misrepresentation theory. These courts have made recovery for buyers easier by interpreting sellers' representations of lawful use as statements of fact rather than law and by lessening buyers' obligations to check records and make other inquiries into the truth of the representations. Some courts have further aided injured buyers by concluding that sellers make implied, actionable representations that existing land uses are lawful by simply offering property for sale or describing its particular uses. These changes have nearly eliminated the required showing of fault and have greatly diminished the requirement that buyers presume seller dishonesty. In some states, this shift has been so radical as to transform the essence of the action from one designed simply to proscribe extreme malfeasance by sellers to one that, devoid of elements of fault, serves to protect a buyer's normal expectations about the quality of the property he is buying. The tort action, in short, has dropped its traditional fault-based background in some states and now resembles a rule defining the minimum standards of merchantable real estate.

With these alterations misrepresentation law can offer considerable protection for normal buyer expectations and can add fairness

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23 *E.g.*, City of Aurora v. Green, 126 Ill. App. 3d 684, 689, 467 N.E.2d 610, 614 (1984); *infra* notes 42-51 and accompanying text.

24 *See infra* notes 42-51 and accompanying text.

25 *See infra* notes 66-69 and accompanying text.

26 *See infra* notes 78-85 and accompanying text.

and efficiency to the land sale process. Yet, as discussed in this section, misrepresentation law can reconcile conflicting buyer-seller interests and can provide relief for all deserving buyers only if eviscerated of all of its elements and stripped of its focus on seller fault. This alteration transforms misrepresentation law from a traditional tort format into something very much like an implied seller warranty. Courts would do better to cease using misrepresentation law as the chief vehicle for providing relief and instead use a contract-based implied warranty action, a formal approach more useful for setting a standard for the presumed quality of all real estate offered for sale.

A. The Shifting Line Between Law and Fact

The long-established law-fact distinction in misrepresentation law is still applied rigorously by some jurisdictions; many other jurisdictions apply the distinction in weakened form. The distinction today is often criticized as artificial[27] and, to an increasing extent, is subject to exceptions and reformulations that transform nonactionable statements of law into actionable statements of fact. This decline in the law-fact distinction[28] reflects a developing judicial consensus that reliance on legal assertions, even assertions made by adversaries, may at times be reasonable and deserving of legal protection.

Two early exceptions to the law-fact distinction were the so-called confidential-relationship and superior-knowledge exceptions. These exceptions provided relief when the parties stood in some relationship of trust or confidence[29] and when the speaker pos-

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27 Courts have justified invoking the law-fact distinction on the ground that a legal assertion is always a statement of opinion because no person, at least without special training, can be presumed to know the law. Another justification offered is that every person is presumed to know the law, which means that a representee cannot be deceived by an erroneous legal statement. Commentators have forcefully criticized such justifications as being factually inaccurate and manifestly inconsistent. *See* PROSSER AND KEETON ON TORTS, *supra* note 16, § 109, at 759; Cavico, *supra* note 17, at 21-24. *But see* Hamming v. Murphy, 83 Ill. App. 2d 1130, 1135, 404 N.E.2d 1026, 1030 (1980) ("[O]ne is not entitled to rely upon a representation of law as both parties are presumed to be equally capable of knowing and interpreting the law.") (citations omitted). Courts have suggested additional justifications. *See, e.g.*, O'Brien v. Noble, 106 Ill. App. 3d 126, 130, 435 N.E.2d 554, 557 (1982) (sellers have no duty to disclose legal restrictions on development because such statements would constitute unauthorized practice of law and "[n]o duty can arise out of a prohibited act").

28 Many courts have expressly or implicitly rejected the law-fact distinction in the context of land use legality disputes. *E.g.*, Carroll v. Gava, 98 Cal. App. 3d 892, 159 Cal. Rptr. 778 (1979); Norton v. Poplos, 443 A.2d 1 (Del. 1982); Ortego v. Lebert, 406 So. 2d 253 (La. Ct. App. 1981); Benson v. White, 72 A.D.2d 627, 420 N.Y.S.2d 785 (1979); Farnsworth v. Feller, 256 Or. 56, 471 P.2d 792 (1970).

29 PROSSER AND KEETON ON TORTS, *supra* note 16, § 109, at 760 (indicating that members of same family, partners, attorney and client, executor and beneficiary of es-

sessed or purported to possess knowledge of the legal matter that was not available to the plaintiff.[30] The superior-knowledge exception covered misstatements by attorneys as well as misstatements by others who, by reason of training and experience, professed special knowledge of the legal consequences of transactions in which they regularly engaged.[31] Some courts recently have undercut the law-fact distinction more completely by concluding that legal assertions can contain actionable implied assertions of fact.[32] For example, a landowner in form offers a legal conclusion when he states that he possesses good title to a land parcel; his assertion, however, can imply the presence of conveyances or other documents necessary to vest title in him that are the basis of his legal conclusion.[33] The landowner's implied assertion that such documents exist can be viewed as an assertion of fact distinct from the legal conclusion.[34] As such, the implied assertion would furnish the grounds for a misrepresentation action.

Some courts have come close to rejecting the law-fact distinction entirely by concluding that legal assertions under some circumstances can reasonably be interpreted as assertions of fact and are

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tate, principal and agent, insurer and insured, and close friends qualify as confidential relationships); Cavico, *supra* note 17, at 25-26.

30 Dettler v. Santa Cruz, 403 S.W.2d 651, 653 (Mo. Ct. App. 1966) (buyer can maintain action for fraud and deceit when seller failed to inform him of zoning violation about which municipal authorities had repeatedly warned seller); Sawyer v. Pierce, 580 S.W.2d 117, 125 (Tex. Civ. App. 1979) (sufficient evidence existed to conclude that sellers knew of limitation on number of trailers on parcel of land and, concomitantly, constraints on profitability of enterprise, but failed to inform buyers); PROSSER AND KEETON ON TORTS, *supra* note 16, § 109, at 760-61; Cavico, *supra* note 17, at 26-29.

31 RESTATEMENT (SECOND) OF TORTS § 545 comment d (1977). *See also* Nantell v. Lim-Wick Constr. Co., 228 So. 2d 634, 637-38 (Fla. Dist. Ct. App. 1970) (complaint for misrepresentation is sufficient when it alleges that broker misstated ease of obtaining zoning change); Peterson v. Auvel, 275 Or. 633, 637-39, 552 P.2d 538, 540-41 (1976) (complaint in misrepresentation action is sufficient when it alleges that broker knowingly misstated binding effect of purchase money agreement).

32 *E.g.*, Sorensen v. Gardner, 215 Or. 255, 261-62, 334 P.2d 471, 474 (1959) (statement that plumbing complies with building code contained implied factual assertion as to existing plumbing). *See* Cavico, *supra* note 17, at 30-32; James & Gray, *supra* note 17, at 494-95. Nonactionable statements of opinion can also contain implied assertions of fact. *E.g.*, Duhl v. Nash Realty, Inc., 102 Ill. App. 3d 483, 489-90, 429 N.E.2d 1267, 1272-74 (1982) (upholding sufficiency of complaint alleging that real estate agents' opinions concerning property's value contained implied assertion about its actual value).

33 RESTATEMENT (SECOND) OF TORTS § 545 comment c (1977); Cavico, *supra* note 17, at 31.

34 When a landowner's statement cannot be construed to contain an implied assertion of a particular fact, it might nonetheless contain an implied assertion that the landowner knows no facts which would belie his legal conclusion, an implication that can be viewed as factual in nature. *See* National Conversion Corp. v. Cedar Bldg. Corp., 23 N.Y.2d 621, 627-28, 246 N.E.2d 351, 355-56, 298 N.Y.S.2d 499, 504-05 (1969); PROSSER AND KEETON ON TORTS, *supra* note 16, § 109, at 760-61; Cavico, *supra* note 17, at 30-31.

therefore actionable.[35] Courts have held, for example, that a statement that property is located within a particular business zoning category is a factual representation rather than a legal one when phrased and presented as a definite assertion rather than an opinion.[36]

Despite these developments, some jurisdictions continue to adhere to the law-fact distinction.[37] Its continued existence may well be attributable to its value in directing attention to the complexity of legal issues involved in land sales and the unreasonableness of relying on legal conclusions made by untrained people. Nevertheless, reliance on legal assertions will seem reasonable in many situations and should receive express legal protection. Some legal issues are within the ken of ordinary sellers. Even with more complex issues, nonlawyer-sellers might have obtained accurate legal knowledge from lawyers, municipal inspectors or officials, or other authoritative sources. Thus, for example, a buyer might reasonably assume that a building owner knows the zoning status of his property, knows that the present use does not violate the terms of easements or covenants of record, or knows whether his building complies with municipal codes.[38] When the legal issue is one like these that di-

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35 *See* Growther v. Guidone, 183 Conn. 464, 468, 441 A.2d 11, 13 (1981) ("To require the representation to be made as a statement of fact . . . is quite different than to require that the statement be factual as opposed to legal. The former requirement focuses on whether, under the circumstances surrounding the statement, the representation was intended and understood as one of fact as distinguished from one of opinion.") (citations omitted); Gartner v. Eikell, 319 N.W.2d 397, 401 (Minn. 1982) (whether statement was one of law or fact is irrelevant in equitable proceeding for rescission of contract for sale of real estate because of mutual mistake concerning zoning); Gardner Homes, Inc. v. Gaither, 31 N.C. App. 118, 120, 228 S.E.2d 525, 526, *cert. denied,* 291 N.C. 323, 230 S.E.2d 675 (1976) (where both parties to real estate contract believed that property was zoned for commercial use, mutual mistake of fact justified rescission).

36 *E.g.,* Barnes v. Lopez, 25 Ariz. App. 477, 544 P.2d 694 (1976); National Conversion Corp. v. Cedar Bldg. Corp., 23 N.Y.2d 621, 246 N.E.2d 351, 298 N.Y.S.2d 499 (1969).

37 *See, e.g.,* Fields v. Life & Casualty Ins. Co., 349 F. Supp. 612, 615 (E.D. Ky. 1972); Mahler v. Paquin, 142 Ga. App. 582, 585, 236 S.E.2d 512, 514, *vacated on other grounds,* 239 Ga. 645, 238 S.E.2d 692 (1977); Frederick v. Bensen Aircraft Corp., 436 S.W.2d 765, 770 (Mo. Ct. App. 1968).

38 On the reasonableness of a buyer's reliance on a seller's statements of lawful use, see *infra* notes 46-58 and accompanying text. Several courts have asserted that a seller not only might know the legality of his land uses but, for purposes of misrepresentation law, is presumed to know or has a duty to know. *E.g.,* Birch v. Ciria, 205 Cal. App. 2d 1, 6, 22 Cal. Rptr. 798, 801 (1962) (no error in lower court finding that seller, who was maintenance man, should have known that building permit was required for reconstruction); Richard v. A. Waldman & Sons, Inc., 155 Conn. 343, 346-47, 232 A.2d 307, 309 (1967) (seller, developer of residential real estate, should have known truth about compliance with zoning ordinance minimum lot size requirements); Bradbury v. Rentz, No. CA 7958 (Ohio Ct. App. May 3, 1984) (available Aug. 24, 1985, on LEXIS, States library, Ohio file) (seller presumed to know of violation of building occupancy certificate). Moreover, a seller at common law is obligated to convey marketable title, an obligation

rectly and personally affects the seller, the seller's legal conclusion seems much more reliable. Moreover, some legal issues — whether, for example, particular electrical wiring comports with a building code — involve the application of relatively clear legal rules to particular facts. A speaker's assertion in such a case reflects as much a specialized knowledge of facts as it does an expert knowledge of law. As the facts become more complex, buyers are increasingly likely to forego investigation and buyer reliance again would seem more reasonable.[39]

A reasonable, careful buyer, in short, might rely on an assertion about the zoning status or code compliance of a parcel as readily and legitimately as he would rely on an assertion that a basement is dry or a septic system fully operational. It is this basic conclusion about the reasonableness of buyer reliance that has motivated many courts to limit the once dominant law-fact differentiation. Of course, legal assertions can be stated with varying degrees of definitiveness ranging from mere conjecture to unqualified conclusion. Reliance may well be unreasonable when a legal conclusion is expressed clearly as an opinion or is otherwise couched in terms suggesting caution or uncertainty.[40] This limitation, however, also applies to factual assertions, which become unreliable and nonactionable when qualified or expressed as opinion.[41] It can easily be retained as a limitation on misrepresentation liability by a court that rejects the law-fact distinction.

B. Inquiry Duties and the Redefinition of Reasonable Buyer Conduct

Like the law-fact distinction, the traditional misrepresentation command for diligent inquiries by buyers to uncover falsity on the part of sellers has met growing judicial resistance. Yet, despite efforts to weaken or abolish it, the command remains a stumbling

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that presumes a seller knows the contents of his title and one that can subject a seller to liability for unmarketable title or for breach of title covenants for some types of unlawful land uses. *See supra* notes 10, 11.

39 *See* James & Gray, *supra* note 17, at 493 ("[A]s the implication of external facts increases, so does the justification for reliance.").

40 RESTATEMENT (SECOND) OF CONTRACTS § 170 (1979); RESTATEMENT (SECOND) OF TORTS § 545 comments a, d (1977); Cavico, *supra* note 17, at 33; James & Gray, *supra* note 17, at 495-96. *Compare* Cooper v. Jevne, 56 Cal. App. 3d 860, 866, 128 Cal. Rptr. 724, 727 (1976) (misrepresentation action lies for statement of opinion if speaker does not honestly or cannot reasonably believe opinion).

41 *See, e.g.*, Duhl v. Nash Realty Inc., 102 Ill. App. 3d 483, 489, 429 N.E.2d 1267, 1272 (1981) ("Statements as to the value of property, particularly statements made by the seller, are often treated as mere expressions and if so intended and understood, fraud may not be predicated thereon."). *See* Prosser and Keeton on Torts, *supra* note 16, at 755-58.

block for buyers in many jurisdictions.[42] The purpose of the original rule requiring reasonable diligence was to discourage negligence by buyers and to promote attention to self interests. The requirement reflected the longstanding rule of commerce that a contracting party cannot assume honesty on the part of those across the table.[43] It reflected as well a belief that a buyer who has ignored easy checks on the accuracy of a statement by a seller presumably considered the statement unimportant and therefore did not detrimentally rely on it. The rule thus served to distinguish cases of actual detrimental reliance from situations in which the buyer viewed the seller's assertion as unimportant and, consequently, suffered no injury from it.[44]

As courts increasingly have required good faith and minimal fairness in commercial settings,[45] they have reduced or abandoned buyer inquiry duties in situations where such duties have operated to sanction deceptive conduct by sellers.[46] Many courts have re-

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42 *E.g.*, Steinberg v. Bay Terrace Apartment Hotel, Inc., 375 So. 2d 1089, 1092 (Fla. Dist. Ct. App. 1979) (following "the oft-quoted, well-settled, broad generalization that a person to whom false representations have been made is not entitled to relief because of them if he might readily have ascertained the truth by ordinary care and attention"); Zeeman v. Black, 156 Ga. App. 82, 87-89, 273 S.E.2d 910, 916-18 (1980) (holding that purchaser did not exercise due diligence under Fair Business Practice Act, GA. CODE ANN. §§ 10-1-390 to 10-1-426 (1982)); Libby Hill Seafood Restaurants, Inc. v. Owens, 62 N.C. App. 695, 698, 303 S.E.2d 565, 568, *cert. denied*, 309 N.C. 321, 307 S.E.2d 164 (1983) ("Where . . . the purchaser has full opportunity to make pertinent inquiries but fails to do so through no artifice or inducement of the seller, an action in fraud will not lie."); Citation Co. Realtors, Inc. v. Lyon, 610 P.2d 788, 791 (Okla. 1980) (upholding trial court's granting of summary judgment motion against purchaser on fraud claim because evidence indicated that purchaser had means of ascertaining truth of seller's statement); PROSSER AND KEETON ON TORTS, *supra* note 16, § 108, at 750-53; James & Gray, *supra* note 17, at 511-17.

43 *E.g.*, Torres v. State Farm Fire & Casualty Co., 438 So. 2d 757, 758-59 (Ala. 1983) (identifying policy underlying rule as discouraging buyers' negligence and inattention to their own interests); PROSSER AND KEETON ON TORTS, *supra* note 16, § 108, at 751-52; James & Gray, *supra* note 17, at 514-15.

44 On the requirement that the seller's statement be sufficiently material to motivate buyer conduct, see PROSSER AND KEETON ON TORTS, *supra* note 16, § 108, at 753-54; James & Gray, *supra* note 17, at 498-502.

45 An example of the judicially imposed requirement that contracting parties act in good faith is Seaman's Direct Buying Serv., Inc. v. Standard Oil Co., 36 Cal. 3d 752, 768, 686 P.2d 1158, 1166, 206 Cal. Rptr. 354, 362 (1984) (covenant of good faith and fair dealing implied in all contracts). *See generally* Burton, *Breach of Contract and the Common Law Duty to Perform in Good Faith*, 94 HARV. L. REV. 369, 404 (1980) (providing extensive citation to cases expressly recognizing a general obligation of good faith performance in every contract at common law).

46 In many recent decisions courts have not required real estate buyers to check municipal ordinances, land title records, or other public records in order to show reasonable reliance. This rejection of mandatory records-search duties now represents the majority view. *See, e.g.*, United States v. Certain Property Located in the Borough of Manhattan, 306 F.2d 439 (2d Cir. 1962); Cousineau v. Walker, 613 P.2d 608 (Alaska 1980); Barnes v. Lopez, 25 Ariz. App. 477, 544 P.2d 694 (1976); Norton v. Poplos, 443 A.2d 1 (Del. 1982); Chapman v. Hosek, 131 Ill. App. 3d 180, 187-88, 475 N.E.2d 593,

quired checks by buyers only when the seller's statements seem questionable or the buyer otherwise receives notice of possible inaccuracies or falsities.[47] Some courts have even abolished all inquiry duties and now bar recovery only when a buyer's actions in failing to uncover the truth seem " 'wholly irrational, preposterous, or in bad faith.' "[48] This approach is consistent with the law's general condemnation of dishonesty and bad faith. Given this general attitude in the law today, duties of inquiry seem inappropriate when a buyer can prove actual reliance and clear consequential injury.

Although on the wane in misrepresentation law generally, the duty to investigate has retained some vigor in the real estate transfer setting when a buyer could have uncovered the falsity of a seller's assertion by checking public records. Thus, many courts still consider reliance unreasonable when a buyer can check a statement's accuracy by reviewing zoning maps, searching deeds and encumbrances of record, or making inquiries of municipal code enforcers.[49] A rationale for such rigid records-search duties is hard to identify, and the rule requiring searches imposes a difficult and unreasonable burden on most real estate buyers. Searches of these sources may appear to be easy in the eyes of judges and lawyers,[50]

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599 (1985); Ortego v. Lebert, 406 So. 2d 253 (La. Ct. App. 1981); Henderson v. D'Annolfo, 15 Mass. App. Ct. 413, 446 N.E.2d 103, *cert. denied,* 389 Mass. 1101, 448 N.E.2d 767 (1983); Gamel v. Lewis, 373 S.W.2d 184 (Mo. Ct. App. 1963); Fox v. Southern Appliances, Inc., 264 N.C. 267, 141 S.E.2d 522 (1965); Asleson v. West Branch Land Co., 311 N.W.2d 533 (N.D. 1981); Niehaus v. Haven Park W., Inc., 2 Ohio App. 3d 24, 440 N.E.2d 584 (1981); Heverly v. Kirkendall, 257 Or. 232, 478 P.2d 381 (1970); Christenson v. Commonwealth Land Title Ins. Co., 666 P.2d 302 (Utah 1983).

47 *E.g.,* Shelton v. Wells, 28 Bankr. 218, 222 (Bankr. E.D. Mo. 1983); Keeshin v. Levin, 31 Ill. App. 3d 790, 796-97, 334 N.E.2d 898, 903 (1975); Fairmont Foods Co. v. Skelly Oil Co., 616 S.W.2d 548, 551 (Mo. Ct. App. 1981).

48 Foster v. Cross, 650 P.2d 406, 411 (Alaska 1982) (quoting Cousineau v. Walker, 613 P.2d 608, 613 (Alaska 1980)). For cases rejecting mandatory buyer inquiry duties in the context of real estate sales, see *supra* note 46.

49 *E.g.,* Steinberg v. Bay Terrace Apartment Hotel, Inc., 375 So. 2d 1089, 1092 (Fla. Dist. Ct. App. 1979) (upholding trial court's denial of purchaser's action for rescission when purchasers did not inspect zoning and building records prior to closing); City of Aurora v. Green, 126 Ill. App. 3d 684, 688-89, 467 N.E.2d 610, 613 (1984) (upholding trial court's dismissal of misrepresentation action when plaintiff could have readily made inquiries to municipal officials); Pakrnl v. Barnes, 631 S.W.2d 436, 438 (Tenn. Ct. App. 1981) (upholding trial court's dismissal of plaintiff's misrepresentation claim because, inter alia, plaintiffs failed to make inquiries of municipal officials despite "ample opportunity" to do so); NRC, Inc. v. Pickhardt, 667 S.W.2d 292 (Tex. Civ. App. 1984) (buyer has no right to rely on statement contrary to recorded title).

50 The longstanding popularity of the ruling in Flureau v. Thornhill, 96 Eng. Rep. 635 (C.P. 1776), reflects a judicial recognition that the title search process is a difficult one. In *Flureau,* the court denied consequential damages to a buyer when the seller, despite his good faith, was unable to deliver good title. The rule "may have stemmed from the notion that English land titles of that day were so uncertain that it was unreasonable to subject a vendor to substantial liability for his title's failure." THE LAW OF PROPERTY, *supra* note 10, § 10.3, at 643. The rule lives on today in the many states that

but such searches often will be difficult and mysterious to the buyer unrepresented by legal counsel or brokers at the time of contract execution . Buyers of desirable property often must move quickly to make purchase offers and have little time before contract execution to undertake records checks and property inspections. Moreover, a buyer who makes an offer that he believes is unlikely to be accepted may not reasonably be expected to engage in expensive inquiries. Astute or well-counselled buyers often contract for warranties or cancellation clauses protecting them against the risk of seller dishonesty, but untrained and unadvised buyers are unlikely to consider such options.[51] When a seller induces buyer reliance by making a false statement, it is unfair to protect him at the expense of a buyer whose conduct is commercially reasonable in comparison to other untrained buyers. A mandatory inquiry rule discourages negligence and inattention on behalf of those who know the rule but is merely a costly trap for the many who are unaware of it.

One reason, perhaps, why many courts have clung to mandatory inquiry rules in the context of real estate sales is that buyers are deemed to have notice for certain purposes of all matters within the record title of the property they are purchasing. Buyers take property subject to easements, covenants, encumbrances, leases, and other matters of record, whether or not they have actual notice.[52] Courts recognizing this notice rule might well apply it unthinkingly to preclude a buyer's reliance on a statement that contradicts a publicly recorded title. This approach has superficial appeal. For example, it does seem reasonable to assume that a buyer with constructive record notice of a restrictive covenant should not be able to claim reliance on the seller's contention that the property is free of restrictions. Such an approach, however, fundamentally misconstrues the rationale of constructive record notice and the policy reasons supporting state recording statutes. Constructive notice

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limit buyer recovery when a seller in good faith is unable to deliver marketable title. *Id.* § 10.3, at 642-43 & n.12. *See* Report, *Residential Real Estate Transactions: The Lawyer's Proper Role—Services—Compensation,* 14 REAL PROP., PROB. & TRUST J. 581, 587 (1979) (title examination "is generally the most important legal work" connected with property sale).

51 Haskell, *supra* note 3, at 642 ("That [a] buyer should obtain an express warranty for his protection assumes a degree of sophistication on the buyer's part which frequently does not exist.").

52 At common law, buyers took only such title as the seller had to convey, which meant that they took the seller's title subject to all outstanding interests held by third parties. Recording acts alter this rule by giving priority to bona fide purchasers for value who take the property without actual, record, or constructive notice of the interests (pure notice approach), who take without notice and record first (race-notice approach), or who simply record first (pure race approach). *See* THE LAW OF PROPERTY, *supra* note 10, § 11.9. Thus, buyers today in all jurisdictions take subject to third party interests that are properly recorded.

rules define the relative rights of buyers of property vis-a-vis third party claimants in the same property.[53] Buyers with actual or constructive notice of interests of third parties take subject to such interests; buyers lacking notice take free of them.[54] Buyers and third party claimants usually will have had no contact with one another, and a reliable central records center is thus essential to advise each of the rights of the other. Constructive notice rules and recording statutes, however, have no bearing on the respective contractual rights and duties of the buyer and seller. They are bound exclusively by the terms of their agreement without regard to the terms and limitations in any documents of record. As against the seller, a buyer who executes a purchase contract is not presumed to know of, much less to accept, the various limitations on the seller's title.[55] The seller's common law duty is to arrive at closing with marketable title.[56] The seller cannot claim that the buyer, by agreeing to purchase the seller's property, has agreed to take it subject to encumbrances or limitations of record unless the contract expressly so provides.[57]

If a seller's assertion as to matters of record is definite in form and apparently reliable, a buyer having no reason to suspect that the assertion is false should be protected when he relies on it. By way of analogy, no records check is required of buyers of personal property. Car buyers, for example, can rely on a seller's representations and need not investigate their accuracy by checking with some gov-

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53 Several courts have held that a buyer with record notice of third-party interests does not have actual notice so as to defeat a misrepresentation action against the seller, even if the buyer has expressly agreed to take the property subject to all restrictions of record. *E.g.*, Fox v. Southern Appliances, Inc., 264 N.C. 267, 269-73, 141 S.E.2d 522, 524-26 (1965) (reversing trial court's dismissal of claim alleging that seller misrepresented that there were no restrictions on property even though property was subject to covenants appearing in record title); Schoedel v. State Bank of Newburg, 245 Wis. 74, 75-77, 13 N.W.2d 534, 535-36 (1944) (upholding trial court's dismissal of defendant seller's demurrer to misrepresentation action; defendants had claimed that at time they allegedly misrepresented that they had first mortgage on property there was another mortgage on record).

54 More precisely, under nearly all state recording acts, buyers without notice who pay fair value for the property take free of unrecorded third party interests, although in about half of the states (race-notice states) they must also record their deeds before the third parties do. In the few pure race jurisdictions, buyers for value with notice take free of unrecorded third party interests if they record first. *See* THE LAW OF PROPERTY, *supra* note 10, §§ 11.9 to 11.10.

55 Absent a contractual provision to the contrary, the seller is obligated to deliver marketable title, which is a title free of all restrictions and encumbrances. *Id.* § 10.12, at 687-89. Some courts recently have held that in normal real estate contracts buyers implicitly agree to take property subject to encumbrances that are readily visible, actually known to the purchaser, or beneficial to the land. *Id.* § 10.12, at 693.

56 M. FRIEDMAN, *supra* note 3, § 4.2, at 318 ("In the absence of agreement otherwise, a buyer is entitled to a 'marketable title.' ").

57 THE LAW OF PROPERTY, *supra* note 10, § 10.12.

ernmental body, with the manufacturer, or with purchasers of identical cars.[58] In sum, the rules of constructive record notice, valuable in establishing buyer-third party rights, have no reasonable application in defining the relative rights of buyers and sellers.

C. The Broadening Concept of Representation

The decline of the law-fact distinction and the increasing judicial rejection of buyer inquiry duties have greatly expanded the circumstances in which a buyer can recover in misrepresentation for false seller statements. Buyer recovery has been further aided by another, potentially more significant development in misrepresentation law: the increasing tendency of courts to construe some seller conduct as tantamount to a verbal representation of some fact, and to interpret a verbal description of property as an implied representation of lawful use.[59] For example, in several jurisdictions a seller who advertises for sale a five unit apartment building has implicitly represented that the buyer can rent all five units consistent with applicable land use restraints.[60] A seller who has publicized income fignres from income-providing property has implicitly represented that the buyer can use the property for such income-producing activities.[61] This broadened definition of an actionable representation

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58 The seller's representations must become part of the "basis of the bargain" between the buyer and seller. *See* U.C.C. § 2-313 (1977). The Code section is silent concerning any affirmative duties of the buyer to investigate. For discussions of what "the basis of the bargain" locution means, see R. NORDSTROM, HANDBOOK OF THE LAW OF SALES § 68 (1970); G. WALLACH, THE LAW OF SALES UNDER THE UNIFORM COMMERCIAL CODE ¶ 11.06[2] (1981); J. WHITE & R. SUMMERS, HANDBOOK OF THE LAW UNDER THE UNIFORM COMMERCIAL CODE §§ 9-2 to 9-4 (2d ed. 1980); 3 WILLISTON ON SALES § 17-5 (4th ed., A. Squillante & J. Fonseca, eds. 1974); *infra* notes 79-82 and accompanying text.

59 *See* PROSSER AND KEETON ON TORTS, *supra* note 16, at 736-37.

60 Kinsey v. Scott, 124 Ill. App. 3d 329, 336, 463 N.E.2d 1359, 1364 (1984). *See* Iverson v. Solsbery, 641 P.2d 314, 317 (Colo. Ct. App. 1982) (seller who unlawfully converts space into extra apartment has duty to disclose illegality to purchaser because such information "materially affects the desirability of the property"); Strickland v. Vescovi, 3 Conn. App. 10, 484 A.2d 460 (1984) (description of property as two family home suggests that two family use would be lawful); Kannavos v. Annino, 356 Mass. 42, 49, 247 N.E.2d 708, 712 (1969) (seller's advertisement of property as suitable for multifamily use generates duty to disclose that such use would be unlawful); Dettler v. Santa Cruz, 403 S.W.2d 651, 656 (Mo. Ct. App. 1966) (statement that dwelling consists of three units that can be separately rented amounts to representation that such rental would be lawful); Rowntree v. Rice, 426 S.W.2d 890, 892 (Tex. Civ. App. 1968) (seller, by advertising and showing property as including swimming pool, implicitly represented that entire pool is within property boundaries). *But see* Creelman v. Rogowski, 152 Conn. 382, 383-84, 207 A.2d 272, 274 (1965) (seller who advertised property as three-unit apartment building when zoning ordinance limited building to two units made no implied representation of lawful use). The current trend is toward the imposition of greater duty toward buyers. *See, e.g.*, Menzel v. Morse, 362 N.W.2d 45 (Iowa 1985); Walter v. Moore, No. 83-183 (Wyo. May 23, 1985).

61 Sawyer v. Pierce, 580 S.W.2d 117, 124-25 (Tex. Civ. App. 1979). *See* Kannavos v.

is similar to the older, well-established rule of misrepresentation law that a speaker who makes a statement must state enough to avoid misleading the listener.[62] A seller who describes an apartment as having five rental units misleads the listener, and therefore makes an actionable misrepresentation, when he fails to add that one or more of the units cannot lawfully be occupied.[63]

This reasoning comports well with the normal expectations of buyers and is a logical extension of misrepresentation principles, When a seller advertises a tavern for sale, a prospective buyer might logically assume that he can lawfully use the property as a tavern.[64] Similarly, when a landowner sells his property in two parcels, a buyer might reasonably assume that the property has been lawfully partitioned.[65] By dropping the need for an express seller statement, this approach would significantly increase the frequency of seller representations and thereby greatly broaden buyer recovery for undisclosed illegal land uses. Indeed, this approach would give rise to seller representations of lawful use in virtually all cases because real estate sellers always describe the property they are offering for sale, whether in writing, orally, or by showing the property to prospective buyers or their agents. Such descriptions convey implied assertions of lawful use because they quite clearly suggest to the average buyer that the buyer can lawfully use the property for the purposes described or demonstrated. In short, this broadened concept of misrepresentation serves the beneficial purpose of bringing misrepresentation law into compliance with normal buyer expectations.

D. Scienter, Reliance, and the Avoidance of Innocent Losses

Even under such a reformulated misrepresentation doctrine, buyers can continue to encounter difficulties in obtaining relief. A buyer still must prove that he actually relied on the seller's statement[66] and that the seller possessed the requisite scienter. Both of

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Annino, 356 Mass. 42, 49, 247 N.E.2d 708, 712 (1969) (description of property as income producing, together with income figures, gave rise to seller's duty to disclose that such use would be unlawful).

62 *See* Kannavos v. Annino, 356 Mass. 42, 48, 247 N.E.2d 708, 711 (1969) (no liability for bare nondisclosure, but party who speaks " 'is bound to speak honestly and to divulge all the material facts bearing upon the point that lie within his knowledge' ") (quoting F. HARPER & F. JAMES, THE LAW OF TORTS § 7.14 (1956)); PROSSER AND KEETON ON TORTS, *supra* note 16, § 106, at 738-39. Kinsey v. Scott, 124 Ill. App. 3d 329, 336, 463 N.E.2d 1359, 1364 (1984).

63 *See* Norton v. Poplos, 443 A.2d 1, 5-6 (Del. 1982) (seller who advertised zoning category of property misleads buyer if he does not add that restrictive covenants limit many of the activities otherwise allowed in zoning category).

64 Bradbury v. Rentz, No. CA 7958 (Ohio Ct. App. May 3, 1984) (available Aug. 24, 1985, on LEXIS, States library, Ohio file).

65 Ogan v. Ellison, 297 Or. 25, 682 P.2d 760 (1984).

66 *See* PROSSER AND KEETON ON TORTS, *supra* note 16, §§ 107-109; James & Gray,

these elements can prove troublesome. In proving actual reliance buyers can encounter difficult factual issues of materiality, causation, and human motivation. To establish the latter element, seller scienter, a buyer must show that the seller intended to deceive him[67] or, at the minimum, that the seller had reason to know that his representation was false or that he lacked sufficient information to know of its truth or falsity.[68] A buyer will often find it difficult to prove the state of a seller's mind,[69] especially if he did not have prolonged contact with the seller. Moreover, proof of scienter can add time and expense to resulting litigation.

These traditional misrepresentation issues of seller intent and actual buyer reliance are harmful and unneeded in the context of land use legality disputes. A seller who knowingly deceives a buyer on the legality of particular land uses clearly deserves little sympathy or protection. Although less clear, there are good reasons why a seller who unknowingly misleads a buyer on such a matter is no

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Misrepresentation—Part I, 37 MD. L. REV. 286, 296-322 (1977); James & Gray, *supra* note 17, at 488-502, 518-22.

67 Traditionally, a plaintiff seeking recovery under a misrepresentation theory had to establish that the speaker intended to deceive the plaintiff; today, many courts impose liability for negligent and even innocent misrepresentation. The imposition of liability for an innocent misrepresentation makes the speaker strictly liable for his statements. *See* PROSSER AND KEETON ON TORTS, *supra* note 16, § 107; James & Gray, *supra* note 66, at 296-322.

68 For cases illustrating the range of legal standards, see, e.g., Carroll v. Gava, 98 Cal. App. 3d 892, 895-96, 159 Cal. Rptr. 778, 780 (1979) (seller liable for negligent misrepresentation when he had no reasonable grounds to believe his statement that property complied with zoning restrictions was true); Cooper v. Jevne, 56 Cal. App. 3d 860, 865-66, 128 Cal. Rptr. 724, 726-27 (1976) (condominium sales agent liable for statement of opinion that condo units were well built if he does not honestly or cannot reasonably believe the opinion); Birch v. Ciria, 205 Cal. App. 2d 1, 5-6, 22 Cal. Rptr. 798, 801 (1962) (seller liable in misrepresentation because he knew building permit was needed to add apartment); Wilson v. Hisey, 147 Cal. App. 2d 433, 438, 305 P.2d 686, 689-90 (1957) (broker liable for negligent misstatement unless he had reasonable grounds to believe statement was true); Richard v. A. Waldman & Sons, Inc., 155 Conn. 343, 346, 232 A.2d 307, 309 (1967) (developer liable for unintentional misrepresentation of compliance with zoning restriction because he should have known of noncompliance); Lively v. Garuick, 160 Ga. App. 591, 593, 287 S.E.2d 553, 555 (1981) (actual seller knowledge required; essence of action is moral fault); Lawton v. Dracousis, 14 Mass. App. Ct. 164, 170-71, 437 N.E.2d 543, 547-48 (1982) (no liability for nondisclosure of building code violations where seller lacks knowledge after reasonably investigating whether building complied with code); Bradbury v. Rentz, No. CA 7958 (Ohio Ct. App. May 3, 1984) (available Aug. 24, 1985, on LEXIS, States library, Ohio file) (seller liable for nondisclosure without any actual knowledge because he should have known of zoning problem); Tennant v. Lawton, 26 Wash. App. 701, 706, 615 P.2d 1305, 1309 (1980) (broker liable for unintentional misrepresentation because he failed "to take reasonable steps to avoid disseminating . . . false information").

69 An example of the difficulty of proving seller intent is provided in Berger v. Limon, 214 Cal. App. 2d 149, 29 Cal. Rptr. 483 (1963). In *Berger*, the appellate court upheld the trial court's determination that the defendant seller did not receive notices of building code violations despite evidence that the seller had been notified on two separate occasions.

more deserving of protection. The issue is a straightforward one: As between a buyer and a seller, both unaware of the illegalities, on whom should a loss fall?

The seller's superior knowledge provides one basis for favoring the injured, innocent buyer over the innocent seller. The seller is likely to know more about the property, its physical characteristics and uses, and its compliance with land use restraints.[70] The seller also will often possess property surveys and title abstracts and will have greater time and opportunity to learn of the legality of existing uses. Even if a seller must investigate whether his property complies with the applicable regulations, his single study is more efficient than requiring all potential buyers to repeat and thus wastefully duplicate the inquiry. Moreover, sellers offering property commonly have weeks or months to prepare to list their property. Buyers, on the other hand, must often present offers quickly and are frequently unfamiliar with local records, regulations, and procedures.

A second basis for favoring the buyer lies with the difficulty of discerning seller knowledge and intent. If innocent losses fall on the buyer, sellers will be encouraged to disavow all knowledge of illegal uses, and the buyer will be left with the difficult investigative task of discerning what information was presented to or was within the reasonable reach of the seller. When a seller has owned a parcel for years, the buyer's investigative task might well be formidable and might be compounded if the seller has departed the area after the sale.

The workings of the typical real estate market and the desirability of avoiding seller-buyer disputes in the first instance also argue for imposing losses and inquiry duties on sellers. The aim of the law in this area should be not simply fair loss allocation but the stimulation of conduct that uncovers the land use illegalities and thereby avoids the losses before contract execution. With their superior knowledge and greater time to act, sellers are better able to perform the needed inquiries. Sellers are also better positioned to make the inquiries because they almost always have access to professional ad-

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70 By presuming that sellers know certain matters concerning their property, some courts have effectively imposed inquiry duties on them. *See, e.g.*, Bradbury v. Rentz, No. CA 7958 (Ohio Ct. App. May 3, 1984) (available Aug. 24, 1985, on LEXIS, States library, Ohio file) (zoning compliance); Dugan v. Jones, 615 P.2d 1239, 1246 (Utah 1980) (" 'An owner is presumed to know the boundaries of his own land, the quantity of his acreage, and the amount of water available. If he does not know the correct information, he must find out . . . .' ") (quoting Sorenson v. Adams, 98 Idaho 708, 715, 571 P.2d 769, 776 (1977)). Moreover, sellers at common law are obligated to convey marketable title; thus, when executing sale contracts, they are presumed to know whether their title is marketable. *See supra* notes 10, 11, 50.

vice on the need for the inquiries and how to perform them. Sellers commonly[71] employ professional real estate brokers who possess substantial knowledge of property law.[72] Buyers also use brokers, but their brokers are usually paid by the sellers and, as a legal matter, owe buyers few, if any, fiduciary duties.[73] Buyers, therefore, cannot rely on their brokers to advise them fully on matters that might undercut a sale and thereby harm the seller's interest.[74] In contrast, sellers benefit from counsel by professional brokers whose own interests match their employers' interests. Finally, many buyers, particularly those purchasing personal residential or small business property, seek independent legal counsel only after they have signed binding purchase contracts.[75] At the time of contract signing, buyers often have received little or no advice on the actions that they should undertake before committing themselves to buy.

In imposing inquiry duties the law ideally should impose them on parties who are likely to learn of them and be well-positioned to fulfill them, thus promoting loss avoidance. Nonlawyers do not know the law, and the imposition of some duty on a class of people is unproductive if not unfair when the affected people do not know of the duty. Judging from the considerable flow of reported decisions, buyers today are not commonly aware of their obligation to make lawful use inquiries and are not advised of their duties by their

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71 *See, e.g.*, Eskridge, *One Hundred Years of Ineptitude: The Need for Mortgage Rules Consonant with the Economic and Psychological Dynamics of the Home Sale and Loan Transaction*, 70 VA. L. REV. 1083, 1118-22 (1984); Report, *supra* note 50, at 585, 590-92.

72 *See* Note, *Unauthorized Practice of Law by Real Estate Brokers in New Jersey: A Call for Compromise*, 2 RUT.-CAM. L. REV. 322, 339-40 (1970) (arguing that real estate brokers should be allowed to provide to clients some services which are now the province of lawyers because of brokers' background in field, their study, and current regulation insuring their competence).

73 For a recent summary of the prevailing view that buyers' brokers are agents or subagents of the sellers, with a discussion of recent decisions obligating brokers to deal fairly with buyers, see Eskridge, *supra* note 71, at 1196-1200. A good recent judicial consideration is Sawyer Realty Group, Inc. v. Jarvis Corp., 89 Ill. 2d 379, 386, 432 N.E.2d 849, 852 (1982) (arguing, inter alia, that "[r]eal estate brokers occupy a position of trust with respect to the purchasers with whom they are negotiating"). *See also* Note, *Real Estate Brokers' Duties to Prospective Purchasers*, 1976 B.Y.U. L. REV. 513, 514-21 (discussing cases holding brokers liable to buyers for breach of duties that arise from fiduciary relationship between buyer and broker or that are imposed by courts as matter of public policy).

74 *See* Eskridge, *supra* note 71, at 1118-24, 1194-1200; Comment, *Dual Ageney in Residential Real Estate Brokerage: Conflict of Interest and Interests in Conflict*, 12 GOLDEN GATE 379, 387 (1982) (arguing that buyer's broker, because he gets share of seller's broker's commission, "has exactly the same financial motivation as the seller's broker to quickly close the deal at any relatively high price").

75 *See* Report, *supra* note 50, at 585. An additional problem is that buyers often never obtain independent legal advice; they seek legal advice, if at all, jointly with the seller. Comment, *Conflicts of Interest in Real Estate Transactions: Dual Representation—Lawyers Stretching the Rules*, 6 W. NEW ENG. L. REV. 73, 73 (1983) ("In many real estate transactions only one attorney is retained and acts for all parties.") (footnote omitted).

brokers. Unless advised, sellers as a class would presumably be equally unaware of such duties. But professional brokers should quickly become aware and should be prompted, in serving their clients' interests as well as their own, to disseminate information and facilitate seller compliance.[76] Because sellers as a class are better advised, the purpose of the law—to avoid innocent injuries by stimulating proper inquiries—is better served by shifting inquiry duties to the seller.

When it is determined that a loss should be imposed on an unknowing seller rather than an unknowing buyer, a seller's knowledge becomes irrelevant. A buyer, accordingly, should not be required to offer proof concerning a seller's scienter. Preferring the innocent buyer in this manner should also relieve him of the need to show that he actually relied on the seller's misstatement.[77] The actual reliance element of traditional misrepresentation law requires the buyer to demonstrate the materiality of the misstatement and his causal reliance upon it.[78] This actual reliance requirement can operate to deny relief to many buyers who have in fact suffered economic loss by purchasing property misdescribed by sellers.

A better approach on the reliance issue may be found in the

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76 *Cf.* Easton v. Strassburger, 152 Cal. App. 3d 90, 101, 199 Cal. Rptr. 383, 389 (1984) (court imposes burden on brokers to inspect property for defects and to disclose material defects to buyers because of "the benefit thus conferred on buyers" and "the relative ease with which the burden can be sustained by brokers").

77 Even under this modification of misrepresentation law, sellers could still point to a buyer's clear lack of reliance as indicating that the buyer did not actually suffer injury.

78 South v. Colip, 437 N.E.2d 494, 498 (Ind. Ct. App. 1982) (misrepresentation must be of material fact and cause plaintiff to act in reliance on it); Diener Enters., Inc. v. Miller, 35 Md. App. 410, 412, 371 A.2d 439, 441 (1977) (" 'Thus it is clear . . . that . . . the plaintiff must show not only that he would not have performed the act from which the injury resulted but for the misrepresentation, but also that the fact misrepresented was the proximate cause of the injury.' ") (quoting Lustine Chevrolet v. Cadeaux, 19 Md. App. 30, 35, 308 A.2d 747, 751 (1973)); PROSSER AND KEETON ON TORTS, *supra* note 16, § 108; James & Gray, *supra* note 17, at 497-502 (discussing materiality), 518-22 (discussing proximate cause).

Misrepresentations that result in small monetary loss or are insufficiently linked to a buyer's essential needs have failed to satisfy the actual reliance element. *See, e.g.*, Evergreen Land Co. v. Gatti, 554 S.W.2d 862, 864-65 (Ky. Ct. App. 1977) (court suggested that misstatements of quantity are material only if they represent more than 10% of property's value); Ollerman v. O'Rourke Co., 94 Wis. 2d 17, 42, 288 N.W.2d 95, 107 (1980) (item is material if reasonable person would attach importance to it or if vendor knows or has reason to know that purchaser is likely to regard the matter as important). *See also* Note, Reed v. King: *Fraudulent Non-Disclosure of a Multiple Murder in a Real Estate Transaction,* 45 U. PITT. L. REV. 877, 891-97 (1984). Courts have also found reliance lacking when the buyer knows the seller's statement is false when executing the purchase agreement or casually fails to pursue available facts that would lead to the discovery of the falsity. *See, e.g.*, Norton v. Poplos, 443 A.2d 1, 6 (Del. 1983); Fairmont Foods Co. v. Skelly Oil Co., 616 S.W.2d 548, 550 (Mo. Ct. App. 1981) (misrepresentation action failed because plaintiff would have discovered limitation on use of property had he been reasonably diligent in making inquiries).

rules governing personal property sales. Under the Uniform Commercial Code, statements by sellers that become a part of the "basis of the bargain" constitute express warranties.[79] If the seller breaches, the buyer may recover without showing either his actual reliance or the materiality of the misrepresentation.[80] This "basis of the bargain" is a distinctly watered-down reliance element and only a slight obstacle for buyers.[81] On its face, the Code denies recovery only for injuries resulting from factual misstatements that are clearly tangential to the buyer's interests and that the parties did not contemplate as any part of their agreement.[82]

This diluted reliance requirement better adjudicates disputes between buyers and sellers of real estate than the traditional, rigorous misrepresentation reliance element. If a buyer suffers damage because a seller misstated a parcel's quality or characteristics, the seller, rather than the buyer, should suffer the loss. If a land use illegality is minor and has little impact on the property's market value, the proper approach is not to deny all relief for lack of materi-

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79 U.C.C. § 2-313 (1977). *See, e.g.*, Slyman v. Pickwick Farms, 15 Ohio App. 3d 25, 472 N.E.2d 380, 385 (1984) (veterinarian's statement about health of race horse prior to sale became part of basis of bargain and, under U.C.C. § 2-313, constituted express warranty).

80 *See* Marston v. E.I. DuPont de Nemours & Co., 23 U.C.C. Rep. 1140, 1142-43 (W.D. Va. 1978) (when seller orally represented that product would control plaintiff's insect problem, no proof of reliance required); U.C.C. § 2-313 comment 3 ("In actual practice affirmations of fact made by the seller about the goods during a bargain are regarded as part of the descriptions of those goods; hence no particular reliance on such statements need be shown in order to weave them into the fabric of the agreement."); J. WHITE & R. SUMMERS, *supra* note 58, § 9-4, at 333 ("Buyer is entitled to legal protection for compliance of goods with *all* of seller's promises and representations . . . even though some may be of relatively small import.") (emphasis in original).

81 *See* D. WHALEY, *supra* note 15, at 34 (comments to U.C.C. § 2-313 "strive mightily to repudiate" the old reliance requirement); J. WHITE & R. SUMMERS, *supra* note 58, § 9-2, at 328 (basis of bargain requirement is "a rather mysterious but much diluted reliance requirement"), 332-39 (collecting case law and commentary on whether Code changes reliance element in warranty actions, concluding that while what Code does to pre-Code law is unclear, next 20 years may nonetheless witness its disappearance); Murray, *"Basis of the Bargain": Transcending Classical Concepts*, 66 MINN. L. REV. 283 (1982) (reviewing dispute among courts and commentators and suggesting "reasonable expectations of the buyer" test as resolution); Comment, *The Meaning of "Part of the Basis of the Bargain,"* 19 SANTA CLARA L. REV. 447, 448-50 (1979) (reviewing three common views of § 2-313 as requiring showing of reliance, no showing of reliance, or establishing presumption of reliance).

82 Under the Code an express warranty is created by "[a]ny affirmation of fact or promise made by the seller to the buyer which *relates* to the goods and becomes a part of the basis of the bargain." U.C.C. § 2-313(1)(a) (1977) (emphasis added). Similarly, "[a]ny description of the goods which is made part of the basis of the bargain creates an express warranty" that the goods will conform to the description offered. U.C.C. § 2-313(1)(b) (1977). The official comment to § 2-313 also indicates that virtually all of the seller's statements constitute express warranties: "all of the statements of the seller [become part of the basis of the bargain] unless good reason is shown to the contrary." *See id.* comment 8. *See also* G. WALLACH, *supra* note 58, ¶ 11.06[2].

ality but to award lesser relief.[83] A buyer should recover even though he possessed information that would have led him to discover the illegal use unless his carelessness is so blatant as to indicate that he considered the seller's statement irrelevant and ignored it when setting his purchase price. When a misstating seller sells his property at a higher price than it would command in a market where all buyers knew of its illegal use, the seller gains an amount equal to the buyer's loss. Little justification exists for allowing the seller to retain this undeserved gain at the expense of a negligent buyer.[84]

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83 Professor Palmer notes that many courts allow restitution for mistakes in the quality or attributes of property being sold only if the mistake is basic or fundamental. 2 G. PALMER, THE LAW OF RESTITUTION § 12.2, at 533-38 (1978). One of the most important facts in determining whether a mistake is basic is its effect on the economic equivalence of the agreed-upon exchange: Rescission is normally allowed only if the mistake resulted in a serious lack of equivalence. *Id.* at 534. Generally, Palmer asserts that this materiality requirement derives from a desire to protect the expectations of contracting parties: "In both business and personal affairs, parties build on their contract expectations, whether by action or inaction, and it is important in a highly organized society that they be able to do so." *Id.* at 533. This desire to protect contractual expectations conflicts with, and must be weighed against, the desirability of achieving a just result free of hardship to one side and undue gain to the other. *Id.* at 533-36. In the case of land use legality mistakes, a materiality requirement is appropriate when a buyer seeks rescission of a real estate sales contract because rescission can considerably upset the contractual expectations of sellers. *See infra* note 159. When the buyer desires or is willing to retain the property and seeks only restitution of excess value paid to the seller, however, a materiality requirement is unnecessary. The contractual expectations of a seller required to pay back part of the purchase price are not significantly frustrated because the sale itself is respected. He is surprised only by having less money on hand, a surprise, of course, that faces every defendant liable for damages. The fairness concern of returning the undue gain to the buyer should prevail in this instance. At bottom, the issue is clear: Is it better to let a seller retain $1,000 because he expected he would be able to do so, or to force the seller to repay the $1,000 because he has been unjustly enriched at the buyer's expense? Finally, it should be remembered that, as the materiality of the mistake decreases, so does the amount the seller must repay.

84 The *Restatement of Restitution* considers the plaintiff's negligence irrelevant in awarding restitution for mistake. RESTATEMENT OF RESTITUTION § 59 (1937). This position is correct given that the rationale underlying a grant of restitution for mistake is simply the avoidance of unjust enrichment. *See* Fuller, *Mistake and Error in the Law of Contracts,* 33 EMORY L.J. 41, 78-79 (1984) ("The entire concept of relief for mistake at American law ultimately may be seen to rest on a basis of unjust enrichment."). Furthermore, it does not unduly upset the finality of contracts to require sellers to disgorge their excess receipts. The exchange of goods at a fair price remains intact.

The buyer's negligence should bar recovery, if at all, only when the buyer seeks contract rescission or other relief that would fully upset the contract and materially disturb the seller's expectations. Professor Palmer argues that a plaintiff's negligence is always relevant in deciding whether rescission should be granted. 3 G. PALMER, THE LAW OF RESTITUTION § 16.3, at 464-65 (1978) ("When a case turns on rescission for mistake in basic assumptions, the negligence of the party seeking relief is always a relevant factor, particularly if he also was the party whose act caused the mistake."). His conclusion, however, may sweep too broadly. Palmer considers only cases in which the plaintiff's active negligence was the sole cause of the mistake, as, for example, when a land buyer erroneously looks at the wrong property or when a bidder miscalculates his bid. *Id.* at 465. Such cases are like cases of simple unilateral mistake, where mistaken plaintiffs are often denied rescission if they acted negligently. *See, e.g.,* Cummings v.

Such a buyer might logically be denied consequential damages,[85] but fairness requires that the seller return his ill-gotten gains to the buyer without regard to the buyer's negligence.

E. The Innocent Seller and the Future of Misrepresentation

The caveat emptor doctrine retains little vigor in states that have modified their misrepresentation law as described above. In its place is a new-faced law of misrepresentation that imposes liability on many sellers who have done little more than sell property containing unlawful land uses. The operation of this new tort law of real estate sales can be illustrated by the plight of a hypothetical buyer of a duplex who fails to determine, after examining the duplex and checking local ordinances, that the building is too small to use as a duplex under local zoning laws.[86] Under traditional misrepresentation law the seller would be liable to the buyer, if at all, only if he knowingly asserted that the existing use was legal and if the buyer was unable to discover the illegality after making diligent inquiries.[87] The fully revised misrepresentation law takes a vastly different tack. Under the developing doctrine of implied representation the duplex owner, by showing the property as a duplex, implicitly represents that it can lawfully be used as such.[88]

Dusenbury, 129 Ill. App. 3d 338, 343, 472 N.E.2d 575, 579 (1984) (rescission allowed for unilateral mistake because plaintiffs were not negligent). When the mistake is not caused by the plaintiff but by unknown information equally available to both sides, courts should grant relief regardless of a plaintiff's negligence in failing to uncover the mistake.

The *Restatement (Second) of Contracts* denies contract avoidance or reformation for mutual and unilateral mistake only if the plaintiff's negligence "amounts to a failure to act in good faith and in accordance with reasonable standards of fair dealings," a standard akin to gross negligence. RESTATEMENT (SECOND) OF CONTRACTS § 157 & comment a (1979). The *Restatement* also provides that a party who consciously contracts with only limited knowledge of the facts bears the risk of the mistake and cannot void the contract. *Id.* § 154(b). *See also id.* §§ 152(1), 153. It is difficult to apply these rules to a case in which both the buyer and seller are ignorant of a major land use illegality. Arguably, the buyer who makes no inquiries has assumed the risk under § 154(b), but such inaction may nonetheless reflect good faith and compliance with standards of normal conduct, thereby entitling him to rescission under § 157. The *Restatement* rules, however, presume that contract avoidance is the normal remedy for mistake. Because this remedy is harsh on sellers, a buyer's negligence or gross negligence could reasonably serve as a limit on that type of relief. If the buyer seeks only restitution, the effect on the seller is much less severe and the buyer's negligence is irrelevant. *See infra* notes 160-64 and accompanying text.

85 *See infra* notes 155-63 and accompanying text.

86 The example is derived from Rosenlof v. Sullivan, 676 P.2d 372 (Utah 1983). A similar set of facts is presented in Strickland v. Vescovi, 3 Conn. App. 10, 484 A.2d 460 (1984) (seller who describes property as two family home implicitly represents that such use is lawful and is liable for innocent misrepresentation).

87 *See supra* notes 42-44, 66, and accompanying text.

88 *See* Rosenlof v. Sullivan, 676 P.2d 372, 373-75 (Utah 1983) (upholding jury verdict for plaintiffs in misrepresentation action); *supra* notes 59-65 and accompanying text.

Courts that modify the law-fact distinction would interpret this representation as an assertion of fact rather than of law, and hence actionable.[89] Under diminished scienter rules, a court would presume that a property owner knows or has reason to know the zoning status of his property and hence automatically has the requisite mental state, even without any actual knowledge of the illegality.[90] A buyer lacking strong reason to suspect that the existing land use is illegal would not be obligated to inspect the public records: He could justifiably rely on the seller's implicit representation.[91] A court would also presume actual buyer reliance[92] in this case since the violation is one that has substantial impact on the parcel's value and implicates its quality.

These presumptions and conclusions virtually eliminate all reference to a seller's fault. The seller is liable, not because he has intentionally misled the buyer, but simply because the property being sold cannot lawfully be used for its obvious, intended purpose. Liability is imposed, that is, simply because the quality of the property does not meet the normal, reasonable expectations of the average buyer. The imposition of such liability reflects a fundamental belief that losses caused by illegal land uses, and hence the duty to detect such illegalities, should routinely be imposed on the seller. In effect, courts that have adopted these changes have modified the normal real estate sales contract by adding an implied seller warranty, actionable without regard to the seller's fault, that existing uses of the real estate do not materially violate any land use regulations.

II

Other Developing Theories of Buyer Relief

Buyers surprised to find that their intended land usages are unlawful have occasionally obtained relief under theories other than misrepresentation. These theories also reflect recent and increasing judicial hostility to caveat emptor and a belief that sellers should be liable for not disclosing known material land use violations and for innocent as well as deliberate misstatements. Several recent decisions expand relief further for buyers and provide additional evidence of a developing judicial sense that innocent sellers should bear unforeseen losses and, by implication, should have the duty to prevent them.

California and Colorado courts have taken the lead in imposing

89 *See supra* notes 27-41 and accompanying text.
90 *See supra* notes 68-70 and accompanying text.
91 *See supra* notes 46-58 and accompanying text.
92 *See supra* notes 77-85 and accompanying text.

on sellers affirmative obligations to disclose matters materially affecting the value of the property.[93] This information disclosure obli-

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93 *E.g.*, Clauser v.Taylor, 44 Cal. App. 2d 453, 454, 112 P.2d 661, 662 (1941) (seller liable for not revealing building erected on a landfill); Cohen v. Vivian, 141 Colo. 443, 447, 349 P.2d 366, 367 (1960) (latent soil defect creates duty of disclosure on seller who is aware of defect). Earlier isolated decisions from other jurisdictions also imposed disclosure duties on selling landowners. *E.g.*, O'Shea v. Morris, 112 Neb. 102, 103-04, 198 N.W. 866, 867 (1924) (upholding trial court's granting of rescission where sellers did not disclose that they did not possess title to portion of lot containing driveway and garage).

Other states have imposed disclosure duties in various circumstances or have denied certain types of relief to sellers who have failed to disclose material facts. *E.g.*, Lively v. Garnick, 160 Ga. App. 591, 595, 287 S.E.2d 553, 555 (1981) (intentional nondisclosure of defect not discernible by purchaser, if undertaken with intent to deceive, is fraudulent); Posner v. Davis, 76 Ill. App. 3d 638, 643-44, 395 N.E.2d 133, 137 (1979) (seller has duty to disclose material latent physical defects known to him); Berman v. Gurwicz, 189 N.J. Super. 89, 92-103, 458 A.2d 1311, 1313-20 (Ch. Div. 1981) (seller has duty to disclose matters materially affecting value of property, but buyers represented by legal counsel cannot be said to have reasonably relied on misrepresentations because counsel should have discovered matter not disclosed); Holcomb v. Zinke, 365 N.W.2d 507 (N.D. 1985) (duty to disclose all material facts which are known or should be known by seller); Millikin v. Green, 283 Or. 283, 285, 583 P.2d 548, 550 (1978) (seller has duty to disclose latent material facts); Shane v. Hoffman, 227 Pa. Super. 176, 185-86, 324 A.2d 532, 536-37 (1974) (duty to disclose occasional sewer back up); Smith v. National Resort Communities, Inc., 585 S.W.2d 655, 659 (Tex. 1979) (seller's failure to disclose flood plain restriction estops seller from demanding contract performance); Ware v. Scott, 220 Va. 317, 320-21, 257 S.E.2d 855, 858 (1979) (intentional nondisclosure of material facts arising after contract execution constitutes fraudulent inducement to perform real estate purchase contract); McRae v. Bolstad, 32 Wash. App. 173, 175-76, 646 P.2d 771, 774 (1982) (seller has duty to disclose water problem); Thacker v. Tyree, 297 S.E.2d 885, 886-88 (W. Va. 1982) (seller has duty to disclose that house was built on filled ground, causing strnctural problems). *See* RESTATEMENT (SECOND) OF CONTRACTS § 161 (1979) (presenting rnles for determining when "[a] person's non-disclosure of a fact known to him is equivalent to an assertion that the fact does not exist").

Several of these jurisdictions, however, have materially qualified the seller's disclosure duty. *E.g.*, Lenzi v. Morkin, 103 Ill. 2d 290, 292-93, 469 N.E.2d 178, 179 (1984) (no duty to disclose substantial increase in tax assessment value of property); Gill v. Marquoit, 269 Or. 581, 585-86, 525 P.2d 1030, 1032 (1974) (no duty to disclose land's susceptibility to flooding); Armentrout v. French, 220 Va. 458, 466, 258 S.E.2d 519, 524 (1979) ("purchaser of real estate must discover for himself the true condition of the premises if he has information which would excite the suspicions of a reasonably prudent person," but seller's efforts to divert attention or to conceal will result in liability) (citation omitted); McPherson v. Purdue, 21 Wash. App. 450, 452-53, 585 P.2d 830, 831-32 (1978) (no duty to disclose serious title defect); Goldfarb v. Dietz, 8 Wash. App. 464, 470-71, 506 P.2d 1322, 1326 (1973) (seller has no duty to disclose nonconforming use status of property because zoning code is rule of law).

Other jurisdictions have repeatedly rejected attempts to impose disclosure duties. *E.g.*, Security Title & Guaranty Co. v. Mid-Cape Realty, Inc., 723 F.2d 150, 154 (1st Cir. 1983) (no duty under Massachusetts law to disclose adverse claim to title); Nei v. Burley, 388 Mass. 307, 310, 446 N.E.2d 674, 676 (1983) (seller has no duty to disclose existence of seasonal watercourse across property). *But see* Danca v. Taunton Sav. Bank, 385 Mass. 1, 7-8, 429 N.E.2d 1129, 1133 (1982) (mortgagee with copy of plot plan disclosing zoning violation implicitly—and negligently—represents to mortgagor who is not shown the plan that no violations exist). Buyers generally are under no obligation to make disclosures to sellers. *See, e.g*, Zaschak v. Traverse Corp., 123 Mich. App. 126, 130, 333 N.W.2d 191, 192-93 (1983) ("Michigan law dictates that a prospective purchaser is

gation applies broadly and includes defects in construction and soil conditions as well as matters wholly external to the property that appreciably affect its value.[94] A highly publicized California decision provides an extreme illustration. The court imposed on the seller a duty to disclose that the property had been the scene of a mass murder several years earlier[95] and allowed the buyer to recover a portion of the purchase price equal to the diminution in value attributable to the incident.[96] Several states have imposed similar disclosure duties on brokers representing real estate sellers.[97]

This disclosure duty is still in its formative stage and remains imprecisely drawn. As applied to date, however, the duty is subject to substantial limits and does not fully protect misled buyers. Sellers generally need disclose only matters of which they have some degree of personal knowledge. Thus, the complicated issue of a seller's knowledge remains a major matter of dispute.[98] Sellers, moreover, need only disclose matters not reasonably ascertainable by the buyer, a limit that denies relief to buyers who should have known the relevant information.[99] Under some formulations of the

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under no duty to disclose facts or possible opportunities within his knowledge which materially affect the value of the property.").

94 *E.g.*, Barnhouse v. City of Pinole, 133 Cal. App. 3d 171, 183 Cal. Rptr. 881 (1982) (soil conditions); Godfrey v. Steinpress, 128 Cal. App. 3d 154, 180 Cal. Rptr. 95 (1982) (termites); Millikin v. Green, 283 Or. 283, 583 P.2d 548 (1978) (roof problem); Shane v. Hoffman, 227 Pa. Super. 176, 324 A.2d 532 (1974) (occasional sewer back-up).

95 Reed v. King, 145 Cal. App. 3d 261, 193 Cal. Rptr. 130 (1983).

96 *Id.*; *see also* Note, *supra* note 78 (discussing this decision and arguing that court defined materiality of nondisclosed fact in manner that was excessively subjective).

97 *E.g.*, Easton v. Strassburger, 152 Cal. App. 3d 90, 99, 199 Cal. Rptr. 383, 387 (1984) (broker duty to inspect for and disclose matters materially affecting value of property); Maples v. Porath, 638 S.W.2d 337, 339-40 (Mo. Ct. App. 1982) (broker potentially liable for failure to disclose termite problem); Neveroski v. Blair, 141 N.J. Super. 365, 373-75, 358 A.2d 473, 477-78 (App. Div. 1976) (broker concealed information about termite infestation; buyer reasonably relied on broker); Crum v. McCoy, 41 Ohio Misc. 34, 38-39, 322 N.E.2d 161, 164-65 (1974) (principals liable for agent broker's concealment of defective sewer); Wilkinson v. Smith, 31 Wash. App. 1, 6-7, 639 P.2d 768, 771 (1982) (broker's personal interest in property); *see* Annot., 8 A.L.R.3D 550 (1966).

98 *E.g.*, Lively v. Garnick, 160 Ga. App. 591, 595, 287 S.E.2d 553, 555 (1981) (seller must know of problem); Shane v. Hoffmann, 227 Pa. Super. 176, 182, 324 A.2d 532, 536 (1974) (actual knowledge, reckless iguorance of falsity, or special duty to know truth imposed because of special circumstances); Thacker v. Tyree, 297 S.E.2d 885, 888 (W. Va. 1982) (seller must be aware of conditions or defects substantially affecting value of property). On the requirement of showing the seller's scienter in misrepresentation law generally, see *supra* notes 66-69 and accompanying text.

99 *E.g.*, Universal Inv. Co. v. Sahara Motor Inn, Inc., 127 Ariz. 213, 215, 619 P.2d 485, 487 (1980) (no duty to disclose electrical code violation that buyer could have discovered through inspection); Cooper v. Jevne, 56 Cal. App. 3d 860, 866, 128 Cal. Rptr. 724, 727 (1976) (facts must not be within reach of buyer through diligent attention and observation); Creelman v. Rogowski, 152 Conn. 382, 385, 207 A.2d 272, 274 (1965) (buyer must prove actual reliance on seller silence); Fairmont Foods Co. v. Skelly Oil Co., 616 S.W.2d 548, 550 (Mo. Ct. App. 1981) (facts must not be discoverable by buyer

duty the seller must also know or suspect that the buyer is acting in ignorance.[100] Different jurisdictions limit relief in other ways. Wisconsin, for example, only imposes disclosure duties on professional sellers.[101] To date, courts imposing disclosure requirements on sellers have considered and rendered decisions in a handful of lawful use cases.[102]

Several states desiring to eliminate or restrict the caveat emptor rule have enacted statutes to provide needed relief. The Texas Deceptive Trade Practices-Consumer Protection Act,[103] for example, imposes liability on sellers and their real estate brokers for misstate-

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in exercise of reasonable diligence); Holcomb v. Zinke, 365 N.W.2d 507 (N.D. 1985) (no duty to disclose matters that would be discoverable by buyer's exercise of ordinary care and diligence). *See also* Libby Hill Seafood Restaurants, Inc. v. Owens, 62 N.C. App. 695, 699-700, 303 S.E.2d 565, 569 (1983) ("A purchaser who is on equal footing with the vendor and has equal means of knowing the truth is contributorily negligent if he relies on a vendor's statements regarding the physical condition of property."). *Compare* Heverly v. Kirkendall, 257 Or. 232, 237, 478 P.2d 381, 383 (1970) (buyer negligence in failing to discern truth is not defense in misrepresentation action).

100 *E.g.*, Warner Constr. Corp. v. City of Los Angeles, 2 Cal. 3d 285, 294, 85 Cal. Rptr. 444, 449, 466 P.2d 996, 1001 (1970) (aside from cases of active concealment and misleading partial disclosure, duty to disclose arises only if speaker knows that facts are not known to or reasonably discoverable by plaintiff); Cooper v. Jevne, 56 Cal. App. 3d 860, 866, 128 Cal. Rptr. 724, 727 (1976) (disclosure duty arises when seller knows that facts are not known to or within reach of diligent attention and observation of buyer).

101 *See* Kanack v. Kremski, 96 Wis. 2d 426, 434, 291 N.W.2d 864, 868 (1980) (noncommercial vendor has no duty to disclose water problem to noncommercial purchaser); Ollerman v. O'Rourke Co., 94 Wis. 2d 17, 42, 288 N.W.2d 95, 107 (1980) (subdivider-vendor must disclose to noncommercial purchaser material facts know to vendor and not readily discernible to purchaser). Both cases noted in Note, *Property—Caveat Emptor—Duty to Disclose Limited to Commercial Vendors*, 64 MARQ. L. REV. 547 (1981). The commercial-noncommercial distinction presumes that buyers have greater confidence in commercial sellers and are more likely to expect honesty and fair dealing from them.

102 *See* Nece v. Bennett, 212 Cal. App. 2d 494, 496-97, 28 Cal. Rptr. 117, 118-19 (1963) (no duty to disclose that conditions in zoning variance not met); Curran v. Heslop, 115 Cal. App. 2d 476, 481, 252 P.2d 378, 381 (1953) (duty to disclose violation of building codes); Barder v. McClung, 93 Cal. App. 2d 692, 697, 209 P.2d 808, 811 (1949) (duty to disclose that garage converted into apartments in violation of zoning ordinance); Denton v. Hood, 122 Ill. App. 3d 813, 818, 461 N.E.2d 1069, 1073 (1984) (no duty to disclose zoning violation); Gamel v. Lewis, 373 S.W.2d 184, 192 (Mo. Ct. App. 1963) (duty to disclose special temporary deferment received under zoning ordinance); O'Shea v. Morris, 112 Neb. 102, 104, 198 N.W. 866, 867 (1924) (fraud in seller's failure to disclose that portion of driveway and garage extended off property when plaintiff did not know and should not have known of situation); Heverly v. Kirkendall, 257 Or. 232, 234-35, 478 P.2d 381, 382-83 (1970) (nondisclosure that garage located partly off property generated implied representation of lawful use); Goldfarb v. Dietz, 8 Wash. App. 464, 470-71, 506 P.2d 1322, 1327 (1973) (no duty to disclose nonconforming use status of property when seller is ignorant of its status). *See also* Lively v. Garnick, 160 Ga. App. 591, 595, 287 S.E.2d 553, 557 (1981) (no duty to disclose that house built so close to property boundary as to violate restrictive covenant and zoning ordinance where seller did not know of violations); Bradbury v. Rentz, No. CA 7958 (Ohio Ct. App. May 3, 1984) (available Aug. 24, 1985, on LEXIS, States library, Ohio file) (discussed *infra* notes 129-31 and accompanying text).

103 TEX. BUS. & COM. CODE ANN. §§ 17.41-.63 (Vernon Supp. 1985).

ments, regardless of scienter, and for knowing nondisclosures of facts.[104] Illinois imposes a similar broad liability on real estate brokers for false statements through the joint operation of its Deceptive Trade Practices and Consumer Fraud Acts.[105] Additionally, Illinois subjects brokers to strict liability for misrepresentations and may have also created broad broker disclosure duties, under the state statute regulating broker licensing and under administrative regulations promulgated by the broker licensing board.[106]

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104 *See id.* § 17.46(b)(5) (misrepresentation of characteristics, uses, etc.), (23) (knowing nondisclosure with intent to induce buyer action). On the application of the Act to real estate sales and brokers, see, e.g., Cameron v. Terrell & Garrett, Inc., 618 S.W.2d 535, 538-40 (Tex. 1981) (buyer is "consumer" of services of seller's real estate agent); Cobb v. Dunlap, 656 S.W.2d 550, 552 (Tex. Ct. App. 1983) (applying Act to knowing nondisclosures before effective date of new subsection barring nondisclosures). *See* Goodfriend & Lynn, *Of White Knights and Black Knights: An Analysis of the 1979 Amendments to the Texas Deceptive Trade Practices Act*, 33 Sw. L.J. 941, 948-50 (1979) (discussing lack of scienter requirement for recovery of actual damages).

A real estate agent liable for misrepresentation may have a defense under the Act if, in making his misstatement, he relied on written false information provided by the seller that the agent did not know and could not reasonably have known was false. TEX. BUS. & COM. CODE ANN. § 17.50B(a)(2) (Vernon Supp. 1985). The Texas statute on fraud in real estate transctions also contains no requirement of seller or broker knowledge of the falsity of the misstatement but does require showings of intent to induce reliance by the buyer and actual buyer reliance. *Id.* § 27.01 (incorporating *id.* § 27.01(a)(1)(A) (Vernon 1968)).

105 Consumer Fraud and Deceptive Business Practices Act, ILL. ANN. STAT. ch. 121 1/2, §§ 261-272 (Smith-Hurd 1984 Supp.); Uniform Deceptive Trade Practices Act, ILL. ANN. STAT. ch. 121 1/2, §§ 311-317 (Smith-Hurd 1984 Supp.). *See* Buzzard v. Bolger, 117 Ill. App. 3d 887, 892-93, 453 N.E.2d 1129, 1132 (1983) (action lies against broker for innocent misrepresentation under the Acts); Beard v. Gress, 90 Ill. App. 3d 622, 625-28, 413 N.E.2d 448, 449-52 (1980) (broker liable for innocent misrepresentation, for concealment and suppression, and for nondisclosure of material facts; diligence of buyer in checking accuracy of misrepresentation is immaterial). The Consumer Fraud Act was amended in 1982 to protect a broker against liability for communicating false, misleading or deceptive information received from the seller unless the broker knows that the information is false, misleading, or deceptive. 1982 Ill. Laws 82-766, § 1, codified at ILL. ANN. STAT. ch. 121 1/2, § 270b(4) (Smith-Hurd 1984 Supp.). The new provision probably cannot fulfill fully its intended purpose because it does not appear to cover broker liability for nondisclosure or concealment or for the misrepresentation of information not provided by sellers. *See* Julian v. Spiegel, 481 N.E.2d 903, 908 (Ill. 1985) (buyer required to present evidence that false information provided by broker did not come from seller).

106 *See* Sawyer Realty Group, Inc. v. Jarvis Corp., 89 Ill. 2d 379, 384-85, 432 N.E.2d 849, 851 (1982) (failure to disclose self-interest in transaction will support implied private cause of action under regulations promulgated pursuant to the Real Estate Brokers and Salesmen License Act, ILL. ANN. STAT. ch. 111, §§ 5701-5743 (Smith-Hurd 1977)); Annot., 28 A.L.R. 4TH 199 (1984). For decisions from other jurisdictions, see, e.g., Menzel v. Morse, 362 N.W.2d 465 (Iowa 1985) (violation by broker of code of ethics provides evidence of negligence in malpractice action); Strauss v. Latter & Blum, Inc., 431 So. 2d 9, 10 (La. Ct. App. 1983) (broker liable for nondisclosure under state deceptive trade practices act if defect known to him) (citing LA. REV. STAT. ANN. §§ 37:1455, 51:1405 (West 1965 & Supp. 1985)); Mongeau v. Boutelle, 10 Mass. App. 246, 247-49, 407 N.E.2d 352, 354-55 (1980) (broker's failure to disclose material fact that could influence buyer is actionable under state deceptive practices act) (citing MASS. GEN. LAWS

Courts should expansively apply these statutes to landowners and brokers selling parcels that violate land use restraints if the buyer is appreciably injured. Given the vagueness of the statutes, however, it is too early to determine what types of land use violations will be sufficiently material to require that they be disclosed and what types of seller or broker statements or conduct will constitute implied assertions of lawful use.[107] These various statutes and decisions, however, do demonstrate a growing willinguess in many jurisdictions to impose liability on sellers and their agents for material misstatements regardless of many of the traditional misrepresentation rules.[108]

The forced disclosure approach largely shifts back to the seller the risk of innocent loss and thus the duty to make inquiries into the legality of existing uses. The limits on mandatory disclosures, however, create uncertainty and restrict considerably the protections afforded buyers. Sellers often need only disclose matters they know. Thus, the disclosure approach can trigger disputes concerning the extent of a seller's knowledge and leaves buyers unprotected against innocent nondisclosures.[109] A court may also deny a buyer relief if the seller reasonably believed that the buyer knew of the illegal uses or if the buyer negligently failed to discover them.[110] Many disclosure duties, moreover, are triggered only by latent material facts, thereby inviting dispute over the materiality of the undisclosed fact.[111] Finally, a breach of the disclosure duty is tantamount only to a misrepresentation that existing uses are lawful; a buyer's recov-

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ANN. ch. 93A, §§ 2, 9 (Michie/Law. Co-op. 1985)); State *ex rel.* McLeod v. C & L Corp., 313 S.E.2d 334, 338 (S.C. App. 1984) (real estate purchasers need not prove elements of common law fraud to prove violation of state unfair trade practices act) (citing S.C. CODE ANN. §§ 39-5-10 to -160 (Law. Co-op. 1985)); Bowers v. Transamerica Title Ins. Co., 100 Wash. 2d 581, 589-90, 675 P.2d 193, 199-200 (1983) (duty arises under state consumer protection act to inform parties to real estate closing of advisability of obtaining independent counsel; here, court applied duty to escrow agent) (citing WASH. REV. CODE ANN. §§ 19.86.010 to .920 (1978)); McRae v. Bolstad, 32 Wash. App. 173, 176, 177, 646 P.2d 771, 774, 775 (1982) (broker has duty under state consumer protection act to disclose matters known to broker; broker must use care to ascertain conditions of property before listing).

107 Applications involving land use illegalities have been few so far. *See, e.g,* Heritage Housing Corp. v. Ferguson, 674 S.W.2d 363 (Tex. Ct. App. 1984) (applying Texas Act to seller of house built one foot over zoning setback line). *See also* Koonce v. Chastain, 674 S.W.2d 484 (Tex. Ct. App. 1984) (applying Texas Act to misrepresentation that certain lots would be restricted to residential use), *aff'd*, 28 Tex. Sup. Ct. J. 509 (1985).

108 *But see, e.g.,* Barnes v. Weitzel, 678 S.W.2d 747, 750 (Tex. Ct. App. 1984) (plaintiff under Texas Act must show actual reliance on misrepresentation).

109 *See supra* note 98 and accompanying text.

110 *See supra* notes 99-100 and accompanying text.

111 *E.g.*, Ollerman v. O'Rourke Co., 94 Wis. 2d 17, 42, 288 N.W.2d 95, 107 (1980) (claim for misrepresentation requires that fact not disclosed or inaccurately related be material; fact is material if reasonable purchaser would attach importance to its existence). *See* Note, *supra* note 78, at 891-97.

ery may still depend on his proving the other traditional elements of misrepresentation law.[112]

Courts have occasionally displayed a willingness to sidestep the traditional elements of misrepresentation law by awarding relief to buyers under rescission and restitution rules.[113] Many courts allow contract rescission in the case of an innocent misrepresentation or a mutual mistake, even in jurisdictions that require in misrepresentation a clear showing of seller scienter.[114] Courts have awarded restitution for unjust enrichment in cases of both intentional and innocent misrepresentation and in cases of mutual mistake.[115]

Traditional principles of rescission and restitution can ameliorate many of the inequitable applications of the longstanding elements of misrepresentation, but the underlying prerequisites of innocent misrepresentation, mutual mistake, and unjust enrichment raise troubling and complex factual questions and are subject to several drawbacks. The principles of rescission and restitution are especially vague, a characteristic that undercuts the ability of parties to rely on probable future events. Moreover, equitable principles do

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112 *See, e.g.*, Berman v. Gurwicz, 189 N.J. Super. 89, 102-03, 458 A.2d 1311, 1319 (Ch. Div. 1981) (requirement that reliance be measured by knowledge gained or which could have been gained by reasonable diligence). *See also* cases cited *supra* at notes 93-95; PROSSER AND KEETON ON TORTS, *supra* note 16, at 737-40; Note, *supra* note 78, at 886-92 (discussing issues of materiality, buyer knowledge, and buyer inquiry duties).

113 *E.g.*, Norton v. Poplos, 443 A.2d 1, 4 (Del. 1982) (facially true statement may constitute actionable misrepresentation if it causes false impression as to true state of affairs, and speaker fails to cure mistaken belief); Dawley v. Sinclair, 419 So. 2d 534, 535 (La. Ct. App. 1982); Gartner v. Eikill, 319 N.W.2d 397, 400 (Minn. 1982) (when parties are mistaken about zoning classification, necessary consent between them is lacking, and purchase agreement is thus invalid); McKay v. McIntosh, 270 N.C. 69, 72, 153 S.E.2d 800, 803 (1967) (trial court's grant of rescission justified when sufficient evidence supported finding that the purchaser's sole interest in buying property was to use it for business and the agent's representation that property was zoned for business induced purchaser's agreement).

On the general trend in contract law to increase the ease with which parties can back out of contracts because of mistake, frustration, or manifest injustice, see G. GILMORE, THE DEATH OF CONTRACT 65-66, 77-83 (1974).

114 *Compare* Sachs v. Swartz, 233 Ga. 99, 103, 209 S.E.2d 642, 645 (1974) (rescission allowed for misrepresentation as to zoning status) *with* Davis v. Northside Realty Assocs., 165 Ga. App. 96, 96-97, 299 S.E.2d 186, 187 (1983) (no damage liability for misrepresentation of zoning status since it is misrepresentation of law).

115 *E.g.*, Norton v. Poplos, 443 A.2d 1 (Del. 1982) (innocent misrepresentation); Dawley v. Sinclair, 419 So. 2d 534 (La. Ct. App. 1982) (innocent misrepresentation); Ortego v. Lebert, 406 So. 2d 253 (La. Ct. App. 1981) (intentional misrepresentation); Gartner v. Eikill, 319 N.W.2d 397 (Minn. 1982) (mutual mistake); MacKay v. McIntosh, 270 N.C. 69, 153 S.E.2d 800 (1967) (innocent misrepresentation); Gardner Homes, Inc. v. Gaither, 31 N.C. App. 118, 228 S.E.2d 525 (1976) (mutal mistake); Slocum v. Leffler, 272 Or. 700, 538 P.2d 906 (1975) (innocent misrepresentation); Sawyer v. Pierce, 580 S.W.2d 117 (Tex. Civ. App. 1979) (intentional misrepresentation). As between the alternate remedies of restitution and rescission, a buyer might logically prefer the former since it would allow him to retain the property with its land use violations while reducing the purchase price to an amount that reflects the property's true fair market value.

not squarely place any duty to investigate on any party and therefore rarely prompt parties to avoid the problem in the first instance. Additionally, the rules provide sellers with only modest incentives to divulge information known to them about the existence of land use violations. Finally, these kinds of relief are often incomplete and, at times, clearly inadequate. Rescission is available only if both parties can be restored to the status quo ante. This resolution is often impossible because a party has acted in reliance upon the finality of the sale.[116] Restitution returns the purchase price to a buyer but fails to reimburse him for even foreseeable consequential damages, which may be his principal loss.[117]

III

TOWARD A NEW IMPLIED WARRANTY OF LAWFUL USE

Many courts, it is clear, are dissatisfied today with the application of the caveat emptor doctrine to real estate sales. They have expressed their dissatisfaction by seizing upon a variety of theories that soften the doctrine's impact on unsuspecting and poorly advised buyers. The theories employed by these courts, however, all suffer from multiple inadequacies. These inadequacies can be best resolved, and the caveat emptor rule best altered, through an approach not yet used expressly by any court: the judicial development of an implied warranty in all real estate sales contracts that

116 *E.g.*, Niesz v. Gehris, 418 So. 2d 445 (Fla. Dist. Ct. App. 1982) (in suit for rescission, buyer must return property and all benefits received); Luciani v. Bestor, 106 Ill. App. 3d 878, 882, 436 N.E.2d 251, 255 (1982) (court sitting in equity will not decree rescission unless both parties can be restored to status quo ante); DePuy v. Bodine, 509 S.W.2d 689, 699 (Tex. Civ. App. 1974) (plaintiff in suit for rescission must ordinarily restore consideration received by him; that is, reestablish status quo of other party). Other limits on rescission also exist. *See, e.g.*, Page Inv. Co. v. Staley, 105 Ariz. 562, 564, 468 P.2d 589, 591 (1970) (by accepting deed after learning of falsity of seller representation as to rezoning possibilities, purchaser ratifies contract and relinquishes right to seek rescission); Rolf's Marina, Inc. v. Rescue Serv. & Repair, Inc., 398 So. 2d 842, 843 (Fla. Dist. Ct. App. 1981) (plaintiff lost right to rescind when he inadvertently ratified contract after discovering zoning problem); Steinberg v. Bay Terrace Apartment Hotel, Inc., 375 So. 2d 1089, 1092-93 (Fla. Dist. Ct. App. 1979) (affirming trial court denial of claim for rescission where plaintiff waited five months before acting); Evergreen Land Co. v. Gatti, 554 S.W.2d 862, 865 (Ky. Ct. App. 1977) (no rescission unless error material); Watson v. Fantus, 275 Or. 605, 610, 552 P.2d 251, 253 (1976) (rescission denied for failure to seek relief promptly). *See also* Lawton v. Dracousis, 14 Mass. App. 164, 172-73, 437 N.E.2d 543, 548 (1982) (where contract was silent on possibility of building code violations and sellers made no representations concerning code, purchaser assumed risk of existence of such violations); Lenawee County Bd. of Health v. Messerly, 417 Mich. 17, 31-33, 331 N.W.2d 203, 210-11 (1982) ("as is" clause in contract for sale of real estate shifted risk to purchaser); DiDonato v. Reliance Standard Life Ins. Co., 433 Pa. 221, 224, 249 A.2d 327, 329 (1969) (when zoning law changed after contract for sale of land completed but before actual conveyance, risk normally allocated to purchaser).

117 For example, when the buyer has moved into the property and must now move out, he may incur substantial relocation expenses.

existing property uses and other uses described by the seller comply with applicable land use restraints.

Such an implied warranty would be a central element of the contract, operating together with express property descriptions, implied title warranties, and, where applicable, implied warranties of habitability and fitness as the critical specifications of the property being conveyed. The implied warranty of lawful use could be altered by the parties and therefore would not unduly restrict the parties' freedom to contract. Upon breach, the warranty would give rise to damages and other relief in accordance with the traditional principles for calculating and limiting contract remedies. Buyers could seek relief for warranty violations both before and after the closing of the sale transaction.[118]

The implied warranty approach offers numerous benefits over the current, uneasy mix of caveat emptor and the palliative rules on misrepresentation and restitution. The implied warranty comports much better than current law with the legitimate expectations of normal buyers that they can lawfully continue existing land uses. The alternative theories available at this time all seek to blame the seller for some fault or mistake. But the legitimacy of the buyer's expectations and the reasons for protecting those expectations are not based on blameworthy conduct by sellers. The issue is not one of fault—the traditional domain of tort law. The issue, rather, relates to the property's characteristics and qualities. The specification of these characteristics and uses is traditionally and legitimately an issue of contract law.[119] A second benefit of the implied warranty

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118 Thus, the implied warranty would not be merged into the deed under the much-discredited (but still surviving) doctrine of merger. *See supra* note 15.

119 The modified misrepresentation action described above is essentially a strict liability tort. Such a tort action, if properly designed, could acbieve the same beneficial results as the implied warranty. Caution should be taken, however, in developing such a tort. First, the duty imposed on a seller should be the duty to disclose rather than a duty to convey property free of illegalities. The seller should be allowed to fulfill his duty by disclosing any illegality to the buyer. *See infra* notes 152-54 and accompanying text. Second, the duty of disclosure should obligate the seller to disclose all illegalities, however slight. Moreover, this duty should obtain regardless of whether the buyer or the seller knows of the illegality. *See infra* notes 159-64 and accompanying text.

A court that undertakes to develop a strict liability disclosure duty of this type should tailor it to match the proposed implied warranty and should not weaken it in a way that undercuts the several benefits of imposing on sellers a clear duty to discover all land use illegalities. This task is feasible, but it will require courts to phrase the disclosure duty in a way that may sound unduly harsh. Courts will need to require sellers to disclose matters of which they are unaware, matters that seem immaterial, and matters of which the buyer is aware. A court could soften the apparent unreasonableness of this duty by holding that a seller has a duty to inspect as well as disclose. This approach would enable a court to assert that a seller unaware of an illegality is at "fault" for failing to discover it, an assertion that may seem more judicious than a contention that his "fault" lies entirely in nondisclosure. Yet, even by combining disclosure and inspection

approach is that it is likely to reduce the incidence of seller-buyer disputes in the first instance. The warranty places losses, and therefore inquiry duties, on the seller, who is better able to make the needed inquiries than is the buyer.[120]

The implied warranty offers substantial advantages over tort-based theories of recovery to both buyers and sellers. For buyers, the warranty provides a broader recovery and eliminates the troublesome issues of knowledge and scienter, materiality, and actual, reasonable reliance. Indeed, as in other breach of warranty actions,

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duties, a court will need to employ seemingly harsh language: It will need to formulate an inspection duty that is satisfied not by a reasonable or diligent inspection but only by an inspection that in fact succeeds in discovering all illegalities. The theoretical problem, of course, stems from the fault-based heritage of tort law. When developing tort liability rules, courts are more comfortable if they can phrase a new rule so that it imposes liability on conduct that appears blameworthy. In this setting, a court developing a tort theory of recovery for buyers would need to impose liability on sellers at times for conduct that lacks this quality. This hurdle can be overcome, as evidenced by the strict liability rules applied in products liability actions. *Cf.* Becker v. IRM Corp., 38 Cal. 3d 454, 213 Cal. Rptr. 213, 698 P.2d 116 (1985) (landlord in business of leasing residential apartments is strictly liable for injuries caused by latent defects in leased premises at beginning of lease term, regardless of landlord's ability to detect them). Contract law, by contrast, has had less concern with seller fault and has long held sellers to strict standards in warranty situations.

A further problem with the tort approach is that normal tort rules for calculating damages are unduly generous in this setting. *See infra* notes 155-58 and accompanying text. Land use illegalities often diminish the value of property only slightly. When the seller is liable because he conveyed property worth marginally less than the sale price, it is unjust to impose on him damages in excess of the lost value attributable to the illegality. Moreover, in many cases illegalities in the property found after the sale of the property can be eliminated by altering the applicable land use standards. Buyers who can obtain such alterations should have their recovery limited to their costs in doing so. A buyer who corrects an illegal condition by repairing or constructing anew should not recover the full cost of repairs or construction when the property, after such activity, is worth more than he paid for it. Consider the case of a property ready for demolition. A recovery under a tort theory based on repair costs is inappropriate because the property's market value is likely to be based entirely on the value of the underlying land. A court would have to manipulate tort theory to achieve a just result in such an instance. Under an approach using a market price differential for calculating damages, however, no recovery would be forthcoming. Even in less extreme cases, the sale price of used real estate reflects its diminished condition.

Finally, the limitations under a tort action begin only when the buyer discovers the illegality. *See, e.g.*, Blum v. Elkins, 369 S.W.2d 810, 813 (Tex. 1963) (limitations period for fraud begins when fraud is discovered or might have been discovered had plaintiff been reasonably diligent). In the context of actions brought after the first few years following the sale, such a limitations rule is appropriate only when coupled with a requirement that the buyer be ousted or the authorities begin to enforce the applicable standard. *See infra* text accompanying notes 168-75.

Even if tailored in this manner, a strict liability tort action may still prove inadequate in a state that does not permit recovery for economic loss in strict liability actions. *See, e.g.*, Moorman Mfg. Co. v. National Tank Co., 91 Ill. 2d 69, 86, 435 N.E.2d 443, 450 (1982). The economic loss limit, however, need not be a problem. The limitation is not applied in misrepresentation actions; by analogy, it need not be applied in this setting.

120 *See supra* notes 70-75 and accompanying text.

the only issue in dispute in many cases is likely to be the issue of damages. For sellers, the warranty imposes broader and more absolute duties but offers to them the clearer rules on modification, waiver, and remedies that typify contract-based recoveries. Sellers would benefit from the clearer contract-based rules on warranty exclusions and limitations periods.[121] They would also benefit from the contract rules limiting buyer recovery to actual out-of-pocket losses and subjecting consequential damage requests to foreseeability rules and mitigation requirements.[122]

The implied warranty offers two other, more public benefits. First, an implied warranty would reduce the pressure on the tort law of misrepresentation by eliminating the need for courts to manipulate the tort's elements to protect sympathetic buyers. Misrepresentation is a tort of broad application, and its traditional elements are reasonable when blameworthy deception is the gravamen of the complaint. Courts anxious to protect injured buyers of real property should not distort these traditional elements without fully considering their value in other situations. The tort of misrepresentation is well suited to disputes over the fault of the speaker or the applicable standards of due care. In contrast, the dispute between a buyer and seller about the lawful use of a parcel relates principally to the quality of the property sold. Transferring this issue from tort to contract, as the implied warranty does, could facilitate the orderly, reasoned development of the law of misrepresentation.

Second, the implied warranty should promote the public interest by enhancing compliance with public land use regulations. Zoning ordinances, building codes, and other restraints serve important public interests, interests that are frustrated by noncompliance. The implied warranty imposes on the seller a duty to identify these public land use restraints and determine whether they are being violated. Current law largely places this task on the buyer, who is less likely to perform it.[123] The implied warranty, by shifting the duty to make inquiries, should therefore improve the identification if not the correction of land use violations.

The judicial creation of the implied warranty of continued lawful use is supported by substantial precedent. Decades ago, courts developed warranties of title in real estate sale transactions and implied them in contracts in which the transferor had employed cer-

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121 *See infra* notes 152-54, 169-74 and accompanying text.

122 *See infra* notes 157-58 and accompanying text.

123 *See supra* text accompanying notes 71-75. It is possible that the implied warranty, by adding visibility to land use restraints, might add pressure for the reform of those that seem outdated or irrational.

tain language of conveyance.[124] More recently, courts have implied a warranty relating to the quality of the property—variously termed a warranty of habitability, fitness, or workmanlike construction—in transfers of new residential property.[125] The development of the warranty of habitability reflects a clear willingness by courts to create new warranty theories where needed to conform property law to widely shared values and expectations. Further evidence of this judicial willinguess to create implied warranties as needed is displayed by the tendency of courts to find implied covenants of good faith and fair dealing in contracts of various types.[126]

Years ago courts also devised implied warranties that reflected the legitimate expectations of parties to transfers of personal property, a process of warranty development that was then continued and refined by legislatures in the Uniform Sales Act and subsequent Uniform Commercial Code.[127] Real property transfer rules have developed more slowly, yet the process of development has clearly begun. An implied warranty of lawful use is an obvious and needed step in this development. Popular expectations and standards of fairness have advanced today to a point where its converse—the caveat emptor rule—is aberrational and anachronistic.[128]

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124 *See* W. RAWLE, THE LAW OF COVENANTS FOR TITLE §§ 1-3, 13-15 (5th ed. 1887). Today covenants of title are not implied in a deed unless the deed employs particular words (such as "warrants") that by statute carry with them implied title covenants. *See, e.g,* ILL. ANN. STAT. ch. 30, § 9 (Smith-Hurd Supp. 1985).

125 *See supra* note 13 and accompanying text.

126 *E.g.,* Seaman's Direct Buying Serv., Inc. v. Standard Oil Co., 36 Cal. 3d 752, 767, 206 Cal. Rptr. 354, 362, 686 P.2d 1158, 1166 (1984) (California law implies in every contract a covenant of good faith and fair dealing); Norgate Homes, Inc. v. Central State Bank, 82 A.D.2d 849, 850, 440 N.Y.S.2d 51, 53 (1981) (covenant of good faith and fair dealing implied in real estate sale contract); Burton, *supra* note 45, at 404 (extensive case citation to states implying such covenants).

127 *See* 2 WILLISTON ON SALES §§ 15-1 to 15-7 (A. Squillante & J. Fonesca 4th ed. 1974); Rasor, *The History of Warranties of Quality in the Sale of Goods: Contract or Tort?—A Case Study in Full Circles,* 21 WASH. L.J. 175, 189-214 (1982) (analyzing development of implied warranties of merchantability and fitness for particular purpose in Kansas both before and after Kansas's adoption of Uniform Commercial Code).

128 Certainly it can be said without fear of contradiction that both case law and legislation during the past fifty years evidence an ever-widening recognition of the idea that *reasonable expectations of purchasers* should not be frustrated. This means, therefore, a corresponding restriction on the seller's freedom of disposition and a recognition of the idea that, in general, the risk of loss should be on the seller if it appears after the sale has been consummated that the subject matter of the transaction is not in all respects as valuable or not as satisfactory for the purchaser's purpose as expected.

Keeton, *supra* note 3, at 1. Keeton was perhaps a bit premature, however, in concluding that, in both real property and personal property sales, "it may be more nearly correct [today] to say *caveat venditor,* or let the seller beware." *Id.* at 2.

For a fine argument that traditional contract law focuses too exclusively on the exact terms of party promises and far too little on party expectations, the social context of contractual dealings, and nonpromissory sources of rights and obligations, see Lightsey,

Although no court has yet implied a warranty of lawful use in a contract tranferring real estate, several courts have manipulated tort law to achieve similar results. In *Bradbury v. Rentz*,[129] the Ohio Court of Appeals imposed liability on a seller of a tavern who failed to disclose to the purchaser that the applicable occupancy certificate limited the building's use to the businesses of bicycle sales and lawn mower repairs. The court eliminated the issue of the seller's knowledge by determining that a selling landowner should know of any zoning restrictions applicable to his property.[130] The court also eliminated the need for any express misstatement of legality by asserting that a seller commits "fraudulent misrepresentation" when he fails to disclose a material fact such as a zoning violation.[131] In effect, the seller was strictly liable simply for having sold property that materially violated land use restraints.

In a similar fashion the Colorado Court of Appeals imposed liability on a seller of property remodeled in violation of applicable building codes. In *Iverson v. Solsbery*,[132] the court stated that each landowner owes a duty to the future owners not to reconstruct or remodel property in violation of building codes.[133] Breach of that duty entitles subsequent owners to damage remedies.[134] The seller's knowledge of the code violations is apparently irrelevant under this liability theory. As in *Bradbury*, the *Iverson* court effec-

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A Critique of the Promise Model of Contract, 26 WM. & MARY L. REV. 45 (1984). Lightsey proposes, as an alternative to the traditional promise model, an exchange-relationship model that determines party rights and duties by looking to general societal norms of fairness and reciprocity and trade customs as well as to the precise party promises.

129 No. CA 7958 (Ohio Ct. App. May 3, 1984) (available Aug. 24, 1985, on LEXIS, States library, Ohio file). A California appellate court employed similar logic in Birch v. Circia, 205 Cal. App. 2d 1, 22 Cal. Rptr. 798 (1962). An owner sold property containing a basement apartment constructed without a building permit and, as such, not lawfully rentable. The seller's description of the property as a multiple dwelling constituted an implicit representation that use of the basement apartment was lawful. The court upheld the trial court's finding that the seller knew of the necessity for obtaining a building permit, pointing to evidence indicating that the seller was a maintenance man.

One decision following a contract law approach is Mayo v. Andress, 373 So. 2d 620 (Ala. 1979), in which the court construed various oral assurances by the seller as contractual guarantees that the property was not subject to any restrictive covenants. The court avoided a potential parol evidence rule problem by concluding that the oral assurances supplemented rather than contradicted the purchase agreement and deed. *Id.* at 624-25. *See also* Warner Constr. Corp. v. City of Los Angeles, 2 Cal. 3d 285, 293-94, 85 Cal. Rptr. 444, 449, 466 P.2d 996, 1001 (1970) (holding city liable in contract for nondisclosure of material facts relating to construction contract where city was immune from tort liability).

130 No. CA 7958 (Ohio Ct. App. May 3, 1984) (available Aug. 24, 1985, on LEXIS, States library, Ohio file).

131 *Id.*

132 641 P.2d 314 (Colo. App. 1982).

133 *Id.* at 316.

134 *Id.*

tively held the seller strictly liable for selling property that violated applicable land use restraints.[135] In short, despite references to seller fraud and unreasonable seller conduct, both courts imposed liability without regard to fault, thereby achieving results similar to those that would be obtained through the implication of a warranty of lawful use.

These two courts and several others have evidenced a clear willingness to manipulate tort law so that results in misrepresentation actions conform with popular values and expectations. Yet, for reasons not clear, these courts have failed to take the next logical step and create a new implied warranty. The explanation for this failure may lie in a judicial belief that implied warranties are unnecessary because parties to sale transactions are always free to insert express warranties into their contracts. Hesitancy based on this belief is unwarranted, however, and inconsistent with recent developments in tort law.[136] Under product liability law, to use a conspicuous example, courts have been willing to expand tort liability to protect the reasonable expectations of buyers even though, in theory, the parties could have inserted warranties in the sale contract.[137] Courts may also perceive that the implication of warranties infringes on the parties' freedom to contract. An implied warranty subject to contractual modification,[138] however, simply conforms the contract to normal expectations and does not seriously infringe on the parties' freedom to agree on contrary terms.

Recently, the Supreme Court of Oregon, in *Ogan v. Ellison*,[139] adopted a contract-based theory of recovery bearing a substantial similarity to the implied warranty of continued lawful use. The defendant in *Ogan* sold property that had not been lawfully parti-

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135 The reasoning adopted by the *Iverson* court logically would impose liability only if the seller is responsible for creating the land use violation: "Moreover, we find it both reasonable and just that the ultimate consequences which result from violation of the building code should be borne by the person who initially perpetrated that violation." *Id.* at 316. Under the court's analysis, the seller's liability rests on the seller's violation of the ordinance rather than on his act of selling. Sellers will often violate ordinances simply by owning property with physical structures that violate zoning codes or other restrictions. A court following *Iverson's* logic might not find such sellers liable if they did not personally engage in the construction that produced the violation. Thus, some sellers would escape liability under such reasoning.

136 For a general consideration of the justification for warranties implied or imposed by law, see Grossman, *The Informational Role of Warranties and Private Disclosure About Product Quality*, 24 J. OF L. & ECON. 461 (1981); Priest, *A Theory of the Consumer Product Warranty*, 90 YALE L.J. 1297 (1981); Schwartz & Wilde, *Imperfect Information in Markets for Contract Terms: The Examples of Warranties and Security Interests*, 69 VA. L. REV. 1387 (1983).

137 *See* PROSSER AND KEETON ON TORTS, *supra* note 16, at 677-724 (describing development of negligence, warranty, and strict liability theories in products liability law).

138 *See infra* notes 152-54 and accompanying text.

139 682 P.2d 760 (Or. 1984).

tioned.[140] The sale gave rise to an implied seller representation that the property had in fact been partitioned as required by statute.[141] The court concluded that this representation resulted in the seller's liability for misrepresentation and fraud upon breach.[142] The buyer, however, had the option of affirming the contract and treating the misrepresentation as a contract breach.[143] In short, the *Ogan* court treated the implied representation as a contractual warranty. The *Ogan* court's reliance on an Oregon statute expressly prohibiting the transfer of property not properly partitioned may limit the decision's precedential value.[144] Moreover, the court did not clearly dismiss seller knowledge as irrelevant.[145] Nonetheless, the decision is perhaps the strongest indication to date of the willingness of courts to provide contractual relief to buyers whose lawful use expectations have been frustrated.

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140 *Id.* at 761-62.

141 *Id.* at 763.

142 *Id.* at 763-65. The *Ogan* court held that the plaintiff's pleadings were sufficient to support breach of contract and fraud claims, *id.* at 765; it remanded the case to the trial court for further proceedings because the court determined that genuine issues of fact remained. *Id.* at 766. In affirming the possibility of tort liability in misrepresentation, the court accepted as true the buyer's allegations that he was ignorant of the illegality and the seller was not *Id.* at 763-65.

143 *Id.* at 763.

144 OR. REV. STAT. § 92.016(2) (1983) ("[N]o person may sell any parcel . . . for which approval of a tentative plan is required. . . ."). Other statutory schemes sometimes provide buyer remedies if land has not been developed properly. *See, e.g,* WASH. REV. CODE ANN. § 58:17:210 (West Supp. 1985) ("All purchasers' . . . property shall comply with provisions of this chapter and each purchaser . . . may recover his damages . . . including any amount reasonably spent as a result of inability to obtain any development permit and spent to conform to the requirements of this chapter. . . .") (cited in Busch v. Nervik, 38 Wash. App. 541, 547, 687 P.2d 872, 876 (1984) (upholding rescission of contract for purchase of land that was not properly platted)).

145 In setting forth its holding, the court assumed that the seller had concealed the lack of partitioning, suggesting that the seller knew of the illegality. *Ogan,* 682 P.2d at 763. Moreover, the court in its misrepresentation and fraud discussion expressly assumed that the plaintiffs had adequately alleged that the seller had such knowledge. *Id.* at 765. The court in its contract breach discussion, however, did not mention the seller's knowledge as an item tbat the plaintiff needed to prove. Such knowledge is normally irrelevant in actions for breach of contract.

The court's proposed approach differs in other ways from the implied warranty set forth in this Article. The court asserted that the buyer was unaware of the illegality. *Id.* at 763. Such an approach interjects an issue—the buyer's knowledge—that is considered irrelevant here. *See infra* notes 160-64 and accompanying text. Moreover, the court distinguished, but did not overrule, its earlier decision in Mitchell v. Chernecki, 286 Or. 285, 593 P.2d 1163 (1979); *Mitchell* held that a purchaser who should have known of zoning ordinance and building code violations could not affirm the contract and obtain damages. *Id.* at 291-92, 593 P.2d at 1166 (discussed in *Ogan,* 682 P.2d at 762-63). Although the *Ogan* court did not discuss damage issues, the plaintiff sought the difference between the value of the property as represented and its value in fact. 682 P.2d at 762. This Article recommends that damages ordinarily be limited to the difference between the purchase price and the value of the property in fact. *See infra* notes 155-58 and accompanying text. The two approaches will not always yield identical results.

A. Scope of the Warranty

In developing the new implied warranty of lawful use, courts will encounter several issues similar to those raised by the new warranties of habitability and residential fitness. Resolution of these issues, however, should not be unduly difficult. The applicability of the new warranty to commercial property and to corporate or other commercial buyers is one issue likely to confront courts early in the development of the warranty. Recently developed warranties of habitability limit the protection of buyers to those purchasing residential property and, in some states, to residential property purchased for the personal use of a noncommercial buyer.[146] The limitation to noncommercial *property* derives from the "habitability" origins of the warranty. This limitation might reflect an awareness of the difficulty of trying to define the minimum fitness or usability of a factory building or other commercial property. Limitation of the implied warranty of habitability to noncommercial *purchasers* is a distinctly minority approach. This limitation evinces a belief that commercial purchasers know more about their needs and rights and can adequately assert them.[147]

Neither limitation comports logically or practically with the implied warranty of lawful use. First, commercial purchasers do not always know more about the need to check land use restrictions. Second, the implied warranty in the commercial context, as in personal and residential property settings, better reflects and protects the normal expectations of buyers. Third, the implied warranty of lawful use in commercial as well as residential settings shifts inquiry duties to the party better able to perform them. Finally, if commercial purchasers may not assert warranty claims, they will turn to misrepresentation relief, with all its attendant complications. The commercial-noncommercial purchaser distinction, in short, lacks any persuasive rationale in this setting and should not be incorporated in the new implied warranty of lawful use.

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146 *See, e.g.*, Conklin v. Hurley, 428 So. 2d 654, 658-59 (Fla. 1983) (implied warranty of fitness and merchantability only extends to improvements physically supporting building); Hopkins v. Hartman, 101 Ill. App. 3d 260, 262-63, 427 N.E.2d 1337, 1339 (1981) (warranty of habitability does not extend to commercial property which includes apartments purchased to produce income); M. Friedman, *supra* note 3, at 47-53. *But see* Hodgson v. Chin, 168 N.J. Super. 549, 553-55, 403 A.2d 942, 944-45 (App. Div. 1979) (warranty applies to building that is part commercial and part residential); Brown v. Sandwood Dev. Corp., 291 S.E.2d 375, 377 (S.C. 1982) (warranty applied to dam and spillway).

147 *See* Hopkins v. Hartman, 101 Ill. App. 3d 260, 263, 427 N.E.2d 1337, 1339 (1981) ("The income-seeker, whether he be purchasing . . . real estate, or any other form of investment, has ample opportunity to investigate, study, appraise, and assess . . . . [T]he [noncommercial] vendee is seeking shelter for himself and his family, oftentimes under considerable pressure.")

It is also inappropriate to limit the warranty of lawful use to sales of noncommercial property. Courts have confined warranties of habitability to residential property for reasons that reflect practical concerns in defining and applying a common law standard of fitness for a commercial structure. The limitation also reflects an assumption that purchasers of commercial property can adequately protect themselves. This assumption is by no means true in the context of lawful use, particularly in the case of purchasers of small businesses and relatively inexpensive investment property. The underlying rationale of the implied warranty does not require that a distinction between commercial and noncommercial buyers be drawn. The increase in awareness of and adherence to land use restrictions obtains in both commercial and noncommercial settings. Moreover, the seller is also the party better able to investigate land use violations regardless of whether the purchaser is a commercial buyer. Finally, the addition of any commercial-noncommercial distinction would be harmful simply because it would add to the factual issues in dispute.

The new implied warranty should include not only existing land uses[148] but any other uses that the seller specifically identifies or describes. The warranty, that is, should transform specific assertions by the seller about the possible uses of the property into express warranties that such uses are lawful. An apartment building owner who asserts that his building can be divided into twenty-three efficiency apartments engages in more than puffing if zoning ordinances limit the building to ten units.[149] A mobile home park seller acts wrongfully if he asserts that the park can accept thirty trailers and county regulations specify a maximum density of fifteen trailers.[150] These seller assertions, if specific in form, should become contractual specifications detailing the quality or characteristics of the property and should give rise to liability under the new warranty

148 A further issue concerning the scope of the warranty will be whether the warranty is violated if the current land use is lawful but the usage is a nonconforming use under zoning ordinances that may prohibit alterations, expansions, and perhaps even major repairs. This issue may require a case-by-case examination, but any nonconforming status appreciably and adversely affecting the property's value should violate the warranty. A seller should be aware that his property is a nonconforming use and, through the operation of the warranty, should be obligated to make an appropriate disclosure. Of course, if no disclosure is made but the buyer nonetheless learns of the status, the buyer presumably will pay only the true market value of the property and therefore will suffer no compensable loss.

149 *See* Steinberg v. Bay Terrace Apartment Hotel, Inc., 375 So. 2d 1089, 1092-93 (Fla. Dist. Ct. App. 1979) (relief denied because of purchaser's lack of diligence in identifying illegality and in seeking relief).

150 *See* Sawyer v. Pierce, 580 S.W.2d 117 (Tex. Civ. App. 1979). *See also* Niehaus v. Haven Park West, Inc., 2 Ohio App. 3d 24, 440 N.E.2d 584 (1981) (misrepresentation that mobile home park will accept 112 units).

if the property fails to conform. This approach, long accepted in the sale of personal property,[151] is equally compelling in the context of real property sales.

In addition to determining how to apply the implied warranty to commercial property and buyers, courts will face a second issue: whether and how the parties by agreement can alter the warranty's terms. In resolving this issue, courts should consider the reasons for the warranty and the nature of the real estate market. The primary purpose of the implied warranty is to induce sellers to discover and disclose land use violations, thereby avoiding buyer-seller disputes.[152] Once disclosure is adequately made, buyers should be able to protect themselves and will not be forced to accept substandard property. Real estate markets are characterized by numerous buyers and sellers with no single seller possessing inordinate market leverage. More importantly, nearly all properties for sale at any time are likely to comply with land use restraints. Thus, buyers should be able to locate another seller and another property when a land use violation renders a property unacceptable.

These considerations suggest that courts should permit the buyer and seller to modify the implied warranty when both know of an existing violation and can appreciate its significance. Full disclosure of violations, therefore, should be allowed in lieu of the warranty. This conclusion does not imply, however, that a seller should be able without full disclosure to exclude the warranty, either by using a blanket exclusion or by way of language that excludes any inconsistency between existing uses and restrictions contained in the property's recorded chain of title.[153] The buyers most in need

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151 *See supra* note 127 and accompanying text.

152 *See supra* text accompanying notes 70-75.

The warranty is principally aimed—although not entirely—at ensuring fairness in dealings between buyers and sellers rather than at larger public concerns such as health and public welfare or the quality of the nation's housing stock. *Compare* Javins v. First Nat'l Realty Corp., 428 F.2d 1071, 1081-82, *cert. denied,* 400 U.S. 925 (1970) (implied warranty of habitability in residential leases, based on concerns over quality of housing, is not subject to waiver or exclusion).

153 Several courts have concluded that an "as is" clause or other general disclaimer in a contract for the purchase of a new residence is not adequate to waive or exclude the implied warranty of habitability. *E.g.,* Davies v. Bradley, 676 P.2d 1242, 1245 (Colo. Ct. App. 1983) ("as is" clause meant that defendant was relieved of obligation to perform further work but was still responsible for quality of work already completed); Briarcliffe West Townhouse Owners Ass'n v. Wiseman Constr. Co., 134 Ill. App. 3d 402, 409, 480 N.E.2d 833, 839 (1985) (express disclaimer of warranties without specific reference to habitability is insufficient; language of disclaimer must "be so clear and so conspicuous that no other reasonable conclusion could be reached but that the buyers read and understood the language"); Schoeneweis v. Herrin, 110 Ill. App. 3d 800, 806-07, 443 N.E.2d 36, 41 (1982) ("as is" language ineffective because agreement containing it did not refer to any particular implied warranty but to implied warranties in general); Sallinger v. Mayer, 304 So. 2d 730, 732 (La. Ct. App. 1974) (waiver of implied warranty

of warranty protection are those who lack adequate counsel. These buyers will likely execute printed purchase contracts containing terms that they do not fully understand. Such form contracts might well come to include blanket exclusions of the lawful use warranty. Moreover, a seller aware that his property materially violates land use restraints might be tempted to include a warranty exclusion, obviating the need to disclose the violation. Both practices would largely subvert the purpose of disclosing land use violations. Indeed, there are no circumstances providing a seller with legitimate grounds for excluding the warranty without a fair disclosure when he knows of existing violations.

Arguably, courts might permit warranty exclusions without disclosure when neither party knows whether land use violations exist. Perhaps, as a matter of freedom of contract, the parties should be free to shift from seller to buyer the duty to inquire and the risk of unknown violations. When the buyer is knowledgeable and capable, such a shift might seem reasonable. Nevertheless, allowing a warranty exclusion when both buyer and seller are ignorant of any violations may result in other, undesirable instances of exclusion. By allowing any warranty exclusion without full disclosure, courts run substantial risks of denying the warranty's protections to buyers less knowledgeable and capable. Moreover, the burdens of inquiry and disclosure are slight and should not unduly burden sellers. On balance, the hazards of allowing warranty exclusions without full disclosure outweigh the slight benefits of contractual freedom that

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against hidden defects must be clear and unambiguous, and evidence at trial must show that waiver was brought to buyer's attention or explained to him). *See* M. FRIEDMAN, *supra* note 3, § 1.2(n), at 53-54. *But see* Schlanger v. Argo Corp., 70 Misc. 2d 864, 866, 335 N.Y.S.2d 174, 176 (1972) (contract clause, containing "as is" language, sufficient to relieve seller of obligation to repair); G-W-L, Inc. v. Robichaux, 643 S.W.2d 392, 393 (Tex. 1982) (language waiving warranty must be "clear and free from doubt" but contract language—" 'no . . . warranties, express or implied, in addition to said written instruments' "—sufficient to waive implied warranty). General disclaimers and other general contract clauses have not been sufficient to protect sellers against liability for misrepresentations as to zoning status. *See* Barnes v. Lopez, 25 Ariz. App. 477, 544 P.2d 694 (1976) (clause saying that property taken subject to all existing ordinances); Zuckerman-Vernon Corp. v. Rosen, 361 So. 2d 804 (Fla. Dist. Ct. App. 1978) (general exculpatory clause); Fox v. Southern Appliances, Inc., 264 N.C. 267, 141 S.E.2d 522 (1965) (clause providing that property taken subject to restrictions of record; misrepresentation as to absence of restrictive covenants). *See also* Lingsch v. Savage, 213 Cal. App. 2d 729, 742, 29 Cal. Rptr. 201, 209 (1963) ("as is" clause does not remove seller's obligation to disclose that property is being condemned). *But see, e.g.*, Lenawee County Bd. of Health v. Messerly, 417 Mich. 17, 331 N.W.2d 203 (1982) ("as is" clause renders purchaser unable to obtain rescission for mutual mistake as to defective sewage system that rendered property uninhabitable under county sanitation code because clause allocated risk of loss to purchaser); Wilkinson v. Carpenter, 276 Or. 311, 314, 554 P.2d 512, 514 (1976) (disclaimer clause undercuts buyer's misrepresentation action in absence of seller fraud).

such exclusions would generate.[154]

B. Damage Calculations and the Role of Materiality and Scienter

Damage calculation issues will also arise under the new implied warranty of lawful use. In actions for breach of the warranty, courts should typically award money damages based on the difference between the property's market value with the violation and the purchase price. This net amount will normally achieve the goal of contract damages of placing the aggrieved party in the same economic position he would have been in had no breach occurred.[155] This method of damage calculation best reconciles the competing interests of buyers and sellers. Moreover, the remedy would eliminate two issues that might otherwise cause trouble—the materiality of the illegal land use and the extent of the purchaser's knowledge of the illegal use at the time of contracting.

In calculating damages for breach of the warranty, courts should compensate buyers for actual economic losses. Thus, injured buyers should not automatically receive damages equal to the costs of altering the purchased premises to bring them into compliance with land use restraints. Even costs actually incurred should not be received as a matter of course.[156] For example, a purchaser of a

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154 One related issue is whether a warranty exclusion must be in writing. An oral disclosure should suffice, although the cautious seller will employ a writing. An additional issue is whether a disclosure is adequate if it identifies a land use practice or condition as a *possible* violation. Such a disclosure, if made in reference to a fairly specific condition or practice, should suffice. Thus, a disclosure by a seller should be adequate if it states that the legality of a particular practice is either unknown to the seller or in doubt. Of course, a seller who expressly disclaims knowledge as to the legality of a practice may be liable in misrepresentation if in fact he knows that the activity is unlawful.

155 *See* J. CALAMARI & J. PERILLO, THE LAW OF CONTRACTS § 14-4, at 521 (2d ed. 1977); Carroll, *A Little Essay in Partial Defense of the Contract-Market Differential as a Remedy for Buyers,* 57 S. CAL. L. REV. 667 (1984). Two recent decisions that follow this approach and compare it to alternative approaches are Loeb Enter. v. Dotsen, 360 N.W.2d 371 (Minn. App. 1985) (misrepresentation as to age of roof; court concludes award of cost of roof replacement would overcompensate plaintiff), and Correa v. Maggiore, 196 N.J. Super. 273, 682 A.2d 192, 197-98 (N.J. Super. Ct. App. Div. 1984) (discussing unfairness of awarding repair costs in many cases).

156 Under the UCC and traditional warranty damage rules, injured parties can recover the difference between the value of the goods as they exist and the value they would have had if they had been as warranted. U.C.C. § 2-714(2) (1977); J. CALAMARI & J. PERILLO, *supra* note 155, at 549-51. In determining the value of goods as warranted, an objective market value standard is used. *Id.* at 550. This measure of damages entails greater liability if the buyer can prove that the contract price was less than the market price at the time of the seller's breach. This element of damage recovery can be ignored when, as will almost always be the case, the buyer keeps the substandard property and does not purchase substitute property. Even when the buyer purchases substitute property, this element is unduly speculative and should therefore be ignored. The only relia-

building with substandard wiring should not routinely receive the full costs of bringing the wiring into code compliance. If the buyer rewires the building, his action may increase its value above the amount paid for it; the buyer should not recover this excess. Only in the instance when the buyer's true economic loss equals the cost of rewiring should a court grant such relief. If the buyer does not rewire, the market value differential provides adequate compensation.

Contract rules requiring buyers to mitigate damages should further limit recovery.[157] Absent fraud by the seller, buyers of property should be obligated to take whatever action seems likely to reduce their losses. Such efforts could include seeking zoning variances or renegotiating private restraints or restrictive covenants. A buyer's duty to mitigate is appropriate when losses are economic in nature and do not stem from the seller's culpable behavior.

Similarly, foreseeability rules should limit the recovery of consequential damages because innocent sellers should not be obligated to take their plaintiffs as they find them.[158] A minor zoning violation, such as the unlawful erection of a front yard fence, should make the seller liable for the cost of removing the fence and any decline in the property's value from what the purchaser paid. If the purchaser for personal reasons finds the lack of a fence unacceptable and incurs expenses in reselling and moving to a new location, the seller should not be liable unless the buyer's response was foreseeable. A buyer who is exceptionally interested in a particular land use should inform the seller of that interest. A limit to damages based on foreseeability in some instances will raise contested factual issues and will thus reduce some of the warranty's simplicity. Such a limitation on the buyer's recovery, however, is fair to both sides. Moreover, this limitation helps justify the shifting of buyer economic losses to unknowing and essentially innocent sellers.

Application of these contract damage rules will eliminate the troublesome question of the materiality of land use violations from a buyer's cause of action. When a land use violation is immaterial in either its market value impact or its effect on the buyer's pricing decision, the buyer will suffer little economic loss under these rules. When this is the case, a court should simply award little damage relief; it need not deny relief entirely just because the buyer's loss is

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ble measure of a parcel's value is the price it brings when offered for sale because real property parcels are not fungible. When dealing with unique goods in local markets, a buyer should not be permitted to contend that the price he agreed to was less than the market price.

157 *See* J. CALAMARI & J. PERILLO, *supra* note 155, §§ 14-15 to -17, at 538-43 (discussing, inter alia, duty to mitigate damages upon breach of contract).

158 *Id.* §§14-5 to -7, at 522-28.

slight. The lack of any need for a materiality requirement can be illustrated by the case of a hypothetical seller who visibly keeps three dogs in his home. Under the proposed warranty, the seller implicitly warrants that the buyer can lawfully keep three dogs there. If zoning ordinances limit the homeowner to two animals, the seller has breached the warranty. The seller's minor breach, however, would give rise to only slight damages, if any, under a market value differential theory of damage calculation. Under traditional tort remedies, by contrast, this seller could face substantial liability if the buyer for peculiar reasons decided to resell the property and move. In misrepresentation law the materiality requirement and other elements can protect the seller from this unexpected and unfair liability. Under the implied warranty, the foreseeability requirement can adequately provide this protection. In this case and others, a foreseeability requirement for consequential damages and mitigation rules can adequately and fairly limit liability without need for an additional requirement of materiality.[159]

These limits on buyer recovery should also eliminate buyer knowledge as an issue in actions for breach of warranty. In misrepresentation actions, a buyer who knows or should know of the falsity of the seller's representation is barred from recovery.[160] This limitation invites dispute over the level of the buyer's knowledge. When damage recovery is limited in the proposed manner, the buyer's knowledge becomes irrelevant.[161] A buyer who knows of land use violations when purchasing is unlikely to pay more for the property than its fair market value with the violation. In such an instance, the buyer has no damages based on the ordinary market-value differential rules. A knowing buyer is also unlikely to incur consequential damages. Even if such damages are foreseeable and thus recover-

159 Materiality will remain important, however, in deciding whether a buyer can rescind the transaction. Rescission normally should only be allowed when justice cannot otherwise be achieved. If the buyer can resell the property, he should be obligated to do so and then seek damages for his loss. If resale is not feasible, however, rescission may be appropriate. For example, when an illegality is so substantial that a buyer would incur sizeable expenditures in bringing the property into conformity for resale, a court should grant the buyer's request for rescission. Rescission under this standard may be appropriate after the sale closing as well as before, even though courts have traditionally been reluctant to grant rescission after closing as a remedy for breach of title covenants. THE LAW OF PROPERTY, *supra* note 10, 810-11. Rescission might be more generously allowed before the sale closing.

160 *E.g.*, Rowntree v. Rice, 426 S.W.2d 890, 893 (Tex. Civ. App. 1968) ("plaintiff in a fraud suit must plead and prove on the merits that he was ignorant of the falsity of the defendant's representations").

161 A buyer's knowledge is irrelevant in actions for the breach of title covenants. *E.g.*, Eames v. St. Paul Title Ins. Co., 654 S.W.2d 560, 561 (Tex. Ct. App. 1983) ("Grantee's actual or constructive knowledge of title defects does not relieve grantor of warranty obligations.") (citation omitted).

able, the buyer is only restored to his pre-purchase position and therefore has no motivation to incur the injuries in the first instance.

The more difficult case in assessing the relevance of buyer scienter is presented by the buyer who negligently fails to discover an illegality and consequently pays an excessive purchase price. Traditional tort law would deny recovery in such a case;[162] the implied warranty of lawful use, by contrast, would provide relief. A negligent purchaser may deserve little sympathy, but contract relief compensates the purchaser only by taking from the seller the premium that the purchaser pays out of ignorance. The seller does not deserve to keep this premium, and restitution for the buyer therefore seems reasonably fair.[163] The deletion of any reference to buyer knowledge or negligence, in short, has no substantial drawbacks. Moreover, it does achieve positive benefits: It encourages seller disclosures by eliminating all the benefits of nondisclosure, and it withdraws a major issue of possible factual dispute.[164]

These various limits on the buyer's recovery may appear parsimonious and overly solicitous of the seller's interests when a seller has engaged in deceitful conduct. For example, when a seller has intentionally deceived a buyer about compliance with an electrical wiring code, elementary fairness might seem to require that the seller pay for rewiring even if the buyer receives a structure worth more than he paid. This sense of fairness stems, of course, from the wrongfulness of the seller conduct. Such wrongful conduct by sellers might justify punitive damages,[165] which contract rules do not

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162 *See supra* notes 42-48 and accompanying text.

163 *See supra* note 84.

When a seller who is negligent in failing to identify an illegality seeks consequential damages as well as recovery of the purchase price – market value differential, the balancing of competing equities becomes more difficult. The issue should be addressed as a question of the adequacy of the buyer's efforts at mitigation. If the buyer could have avoided his loss through reasonable efforts at mitigation and negligently failed to do so, the loss capable of mitigation should not be compensated. A buyer should be held negligent, however, only if he had clear notice of problems and failed to respond reasonably. Broader inquiry duties should not be imposed.

164 A buyer's negligence may be relevant to an inquiry into the determination of damages in some circumstances. If a buyer ignores obvious evidence of unlawful use, he arguably considered the issue irrelevant in setting the purchase price and therefore suffered no loss from the illegality. *See supra* note 83 and accompanying text. This circumstance might arise, for example, if the buyer intends to discontinue the use. The issue might be relevant in calculating what, if any, damages the buyer sustained. Moreover, where the buyer is on notice of a possible illegality by reason of an express statement by the seller that a particular land use is in doubt, the seller may have made an adequate disclosure. *See supra* note 154.

165 *See, e.g.*, Godfrey v. Steinpress, 128 Cal. App. 3d 154, 180 Cal. Rptr. 95 (1982) (recovery of punitive damages and damages for severe emotional distress); Walker v. Signal Cos., 149 Cal. Rptr. 119 (1978) (punitive damages); Millikin v. Green, 283 Or. 283, 583 P.2d 548 (1978) (punitive damages); Lundin v. Shimanski, 124 Wis. 2d 175, 368 N.W.2d 676 (1985) (punitive damages). For a recent judicial discussion of the avail-

provide.[166] To fill this need, courts can and should apply the tort law of misrepresentation as an alternative form of relief in such instances. In this limited role, however, the law of misrepresentation should be retained in a form that preserves its traditional focus on actual deception by sellers.[167]

C. Breach and Recovery

A final issue that courts will face in defining the new implied warranty is when and how the warranty is breached and who can sue for relief. Courts developing other warranties have confronted similar issues. For example, courts expounding the implied warranty of habitability have chosen a statute of limitations, decided when the statute begins to run, and determined whether subsequent purchasers can sue on the original warranty.[168] This section addresses this issue. It considers as well the related question of whether a warranty beneficiary should receive damage relief in the absence of some effort by a third party to halt the illegal property use.

These issues are not subject to a facile resolution. This section proposes a resolution to them, however, that is relatively easy to apply and that respects the competing interests of buyers and sellers of property. The resolution proposed is framed with a view towards

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ability of tort remedies for contract breaches, see Seaman's Direct Buying Serv., Inc. v. Standard Oil Co., 36 Cal. 3d 752, 774-84, 206 Cal. Rptr. 354, 366-73, 686 P.2d 1158, 1170-77 (1984) (Bird, C.J., concurring and dissenting).

166 *See* J. CALAMARI & J. PERILLO, *supra* note 155, § 14-3, at 520 ("Traditionally . . . punitive damages are not awarded in contract actions, no matter how malicious the breach.") (citations omitted).

167 When misrepresentation law is used simply to supplement the implied warranty, courts should retain some of the traditional misrepresentation elements with their focus on the seller's fault. Courts should impose tort liability only for an express seller representation—as opposed to a representation implied from the showing of the property—and should require some demonstration of the seller's scienter and perhaps actual reliance by the buyer. The traditional law-fact distinction and inquiry duties that are placed on buyers should not be retained even after creation of an implied warranty. Many injured buyers, of course, will seek relief under both warranty and misrepresentation theories. In some individual cases the request for relief based on the two claims might eliminate the simplicity benefits achieved by a warranty-based cause of action. Clear warranty liability, however, should encourage sellers to settle, thereby leading to the resolution of most disputes. A separate finding of tort liability will be helpful only to a buyer who has incurred unforeseeable consequential damages or who possesses a legitimate claim for punitive damages. These cases should be few in number.

168 *See* Mallor, *supra* note 13, at 366-75 (discussing cases extending and refusing to extend protection to subsequent purchasers); Note, *supra* note 13, at 479-501 (examining possible defenses to implied warranty claims, including whether warranty has expired); Note, *Builders' Liability for Latent Defects in Used Homes*, 32 STAN. L. REV. 607, 610-21 (1980) (discussing subsequent purchasers' common law and statutory remedies); Comment, *Liability of the Builder-Vendor Under the Implied Warranty of Habitability—Where Does It End?*, 13 CREIGHTON L. REV. 593, 599-602 (1979) (discussing court decisions fixing limitations periods and establishing rules for determining when applicable period begins to run).

the underlying purposes of the warranty. One key aim of the warranty is to protect a buyer's legitimate assumption that a land use is lawful and to eliminate the need to make inquiries on the subject. This assumption merits some form of long-term protection since a buyer may use his lands for many years before a third party enforcer disrupts his possession. The seller's interests, on the other hand, are best served by a limited and definite limitations period and clear limits on his potential liability for avoidable losses.

Title warranty rules suggest a resolution of these competing interests. Title warranties or covenants are of two types: those breached, if at all, upon conveyance and those breached upon an "ouster" of the warranty beneficiary.[169] For this latter type of warranty, the limitations period begins at the time of ouster.[170] Warranties of this type run with the land—at least prior to an ouster—and former owners cannot enforce them.[171] The limitations period for the former type of warranty begins to run from the date of conveyance;[172] these warranties do not run with the land, although subsequent purchasers may have rights to bring actions for their breach.[173]

An analgous bifurcation of the warranty of lawful use would reconcile the competing interests of buyers and sellers without excessive complication. Courts can tailor the warranty to provide for two distinct forms of breach. Each type of breach would give rise to a separate action subject to a distinct limitations period. A breach occurring upon initial conveyance would entitle the purchaser to recover damages based on the diminished market value of the property. No third-party disturbance or ouster would be required for this sort of claim. The limitations period for such a breach should parallel the normal contract breach period and would begin to run upon conveyance without regard to the buyer's knowledge or discovery. This aspect of the warranty would not run with the land, but the right to seek relief would run to subsequent purchasers absent an express provision in the subsequent purchase agreement reserving the right of relief to the seller.[174] A second, alternate action

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169 The covenants breached, if at all, upon conveyance are the covenants of seisen, right to convey, and freedom from encumbrances. The covenants that are breached only upon ouster or eviction are the covenants of quiet enjoyment, warranty, and further assurances. THE LAW OF PROPERTY, *supra* note 10, § 11.13.

170 *Id.* at 815.

171 *Id.*

172 *Id.* at 814.

173 *Id.* at 814-15. A subsequent purchaser may have a cause of action if a court construes a subsequent grantee's deed as containing an implied assignment of a cause of action arising from the breach of a covenant made to a prior grantee. *Id.*

174 *See, e.g.*, Aronsohn v. Mandara, 98 N.J. 92, 99-100, 484 A.2d 675, 678-79 (1984) (when contract contains no prohibition on assignment, contractor's implied warranty of

would require that the buyer show an enforcement or "ouster" and would be subject to a limitation period beginning at that time. The latter aspect of the warranty would run with the land, passing automatically to subsequent takers of the property.

A warranty of lawful use, structured in this fashion, respects the interests of buyers and sellers.[175] A buyer who acts promptly will recover market value losses without having to prove that he was ousted. If the limitations period has run and no ouster has occurred, the buyer cannot recover. But enforcement in such a case is unlikely and the buyer's loss speculative. Furthermore, if ouster does occur later, the buyer is still protected. In practice the warranty will offer some protection to the buyer who learns of the illegalities after the initial limitations period but before any third party enforcement, as might happen, for example, when the buyer seeks to resell and undertakes his own inquiries that turn up illegalities. The warranty does not provide a buyer with a cause of action in such an instance, but the buyer has some bargaining leverage to negotiate for some relief from the initial seller. The buyer can negotiate by offering the seller the opportunity to end exposure to the seller's potential indefinite liability as an inducement to settle.

Under the warranty the seller's possible liability does extend in time almost without limit. Such exposure, however, does not differ from a seller's possible liability under certain covenants of title. Moreover, both the prospect of liability and the amount of any actual liability are likely to diminish substantially after the initial limitation period. Thereafter, the seller will be liable only upon third party enforcement. If enforcement of the restraint is unlikely, the seller's risk of loss will be low and the buyer's negotiating strength slight. The seller might still desire to end all doubt, but the settlement amount will presumably decline with the reduced risk of enforcement.

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good workmanship is automatically assigned as contract right to subsequent purchasers).

175 By comparison, a large number of courts have concluded that the implied warranty of habitability extends for a reasonable period of time and that subsequent purchasers during that period enjoy the benefits of the warranty, even though they are not in privity with the builder or contractor. *See, e.g.*, Blagg v. Fred Hunt Co., 272 Ark. 185, 612 S.W.2d 321 (1981); Redarowicz v. Ohlendorf, 92 Ill. 2d 171, 441 N.E.2d 324 (1982); Keyes v. Guy Bailey Homes, Inc., 439 So. 2d 670 (Miss. 1983); Hermes v. Staiano, 181 N.J. Super. 424, 437 A.2d 925 (1981); Elden v. Simmons, 631 P.2d 739 (Okla. 1981); Gupta v. Ritter Homes, Inc., 646 S.W.2d 168 (Tex. 1983); Moxley v. Laramie Builders, Inc., 600 P.2d 733 (Wyo. 1979). *But see, e.g.*, Wright v. Creative Corp., 30 Colo. App. 575, 498 P.2d 1179 (1972); Governors Grove Condominium Ass'n v. Hill Dev. Corp., 36 Conn. Supp. 144, 414 A.2d 1177 (1980); Navajo Circle, Inc. v. Development Concepts Corp., 373 So. 2d 689 (Fla. Dist. Ct. App. 1979); Oates v. JAG, Inc., 66 N.C. App. 244, 311 S.E.2d 369 (1984), *rev'd*, 333 S.E.2d 222 (N.C. 1985).

CONCLUSION

In numerous decisions over the past decade, state courts across the country have sympathized with the plight of the unknowing buyer of property that violates some land use restraint. They have eroded, unevenly but steadily, several of the traditional barriers to the recovery by buyers of damages under the tort of misrepresentation. Nearly all states have accepted one or another of several major alterations of established misrepresentation doctrine. In the few states that appear to have accepted them all, courts have altered dramatically the face and aim of the misrepresentation action. They have imposed liability on sellers, not based on blameworthy, misleading conduct, but simply because the seller has sold property that cannot lawfully be used for its obvious, intended purpose and that therefore fails to satisfy the normal, reasonable expectations of buyers. They have, in effect, come very close to creating in normal real estate contracts an implied seller warranty that existing property uses comply with applicable land use restraints.

Other judicial and legislative developments reflect this same growing concern for the plight of the unknowing buyer. Several courts have broadened seller disclosure duties so as to require sellers to speak in the face of material violations. State consumer fraud statutes have been construed to impose similar disclosure duties and to create misrepresentation-like damage actions that remove some of the major impediments to buyer relief. Courts have further shown their concern by expanding the availability of restitution and rescission.

The traditional common law rule of caveat emptor has become anachronistic. It requires buyers to detect land use violations when this often-difficult investigative task is better imposed on real estate sellers. Sellers are better situated to know of violations or detect them and have more time to do so; sellers are generally better advised of their legal duties and, as a result, are more likely to fulfill them. For reasons of practicality and fairness, the law should require sellers to detect and disclose to buyers any existing land use violations and should hold sellers liable if they misstate the permissible uses of property offered for sale.

The tort rules on misrepresentation, however, as well as the other remedial actions used by courts to give relief to buyers, are ill-suited for this task. A better way to impose this inquiry and disclosure duty on sellers and to protect the reasonable expectations of buyers is to create an implicit warranty that existing uses of the property, and other property uses described by the seller, are consistent with applicable land use restraints.

This new warranty would operate much like current title cove-

nants and warranties of habitability. In designing the warranty, courts should apply it to all types of real estate sales, not just to sales of residential property. They should allow contracting parties to alter the warranty, but only by way of disclosures by sellers of particular land use violations and not through the use of blanket waiver clauses. They should not require a buyer to prove that he has been disturbed in his possession by reason of the land use violation unless the normal contract statute of limitations has expired and disturbance or ouster seems unlikely. Finally, courts designing the new warranty should normally limit damage recovery to the difference between the amount paid by the purchaser and the market value of the property as it exists, allowing additional damages only if foreseeable and not capable of mitigation.

Courts years ago began creating warranties applicable to personal property sales to bring the law into conformity with shared values and expectations. The same process—begun with the now firmly entrenched and highly regarded warranty of habitability—should be undertaken in the setting of real estate sales. The judicial development today of an implied seller warranty of lawful use, an appropriate and needed step, would eliminate many harsh applications of the caveat emptor doctrine and would align the centuries-old law of real estate sales with contemporary public expectations.