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Property Condition Disclosure Forms: How the Real
Estate Industry Eased the Transition from *Caveat Emptor*
to “Seller Tell All”

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PROPERTY CONDITION DISCLOSURE FORMS: HOW THE REAL ESTATE INDUSTRY EASED THE TRANSITION FROM CAVEAT EMPTOR TO "SELLER TELL ALL"

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PROPERTY CONDITION DISCLOSURE FORMS: HOW THE REAL ESTATE INDUSTRY EASED THE TRANSITION FROM *CAVEAT EMPTOR* TO “SELLER TELL ALL”

George Lefcoe*

*Editors’ Synopsis: This Article recounts the common law evolution away from *caveat emptor* in the sale of residential real estate and how some courts began holding brokers liable for seller errors and omissions. Amorphous, court-imposed disclosure requirements invited fact-laden trials with unpredictable outcomes, as litigators wrestled over what information was “material,” “latent,” “known to the seller or broker,” and inaccessible to the buyer. The real estate industry developed a new protocol requiring sellers to disclose known defects in order to cut back on its own expanding liability, to assist buyers to become fully informed about the property before committing to a purchase, and to clarify for sellers exactly what they need to disclose. This Article reviews the issues brokers have resolved in establishing this near-universal regime of property condition disclosure forms, including the selection of the best institution to create and modify the forms, the topics that should be covered, whether compliance should be deemed waivable, and whether sellers should pay for property inspections. Finally, the Article evaluates California’s Natural Hazard Disclosure Law, a statute that requires sellers, regardless of personal knowledge, to disclose the existence of area-wide natural and man-made hazards.*

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I. INTRODUCTION

The house architecture of the 1950s and 1960s, known generically as “mid-century,”¹ has now become a favorite of home buyers, design aficionados, and the historic preservation crowd. While 1950s house architecture has returned to the height of fashion, real estate disclosure law has

¹ See, e.g., MID-CENTURY ARCHITECTURE IN AMERICA: HONOR AWARDS OF THE AMERICAN INSTITUTE OF ARCHITECTS, 1949-61 (Wolf Von Eckardt ed., 1961).

changed significantly in the past half century.

Home sellers in the 1950s had no obligation to mention property defects to buyers as long as they resisted the temptation to conceal latent defects or to lie about the condition of the property.² To become liable for concealment, sellers would have needed to do more than just keep quiet: they would have needed to do something such as placing a mattress over a gaping hole to hide dry rot and termites³ or painting over water stains from an unrepaired roof leak.⁴ As one commentator put it, in those days, sellers' lawyers could reasonably have copied a page from *Miranda* and counseled their clients: "You have the right to remain silent. Anything you say can and will be used against you during the contract negotiations."⁵

In a typical pre-1950s case, the Massachusetts Supreme Judicial Court rejected a disappointed buyer's claim for relief, made after the buyer discovered his newly purchased home was termite-infested.⁶ The tight-lipped seller had known about the infestation but had said nothing to the buyer. Hewing somewhat reluctantly to the prevailing "rule of nonliability for bare nondisclosure," the court declared: "The law has not yet, we believe, reached the point of imposing upon the frailties of human nature a standard so idealistic as this. That the particular case here stated by the plaintiff possesses a certain appeal to the moral sense is scarcely to be denied."⁷

By the mid-1960s, the consumer-protective norms applicable to the sale of goods were being applied to the sale of homes for the protection of home buyers. In all but a few states—with Massachusetts still among the holdouts⁸—home sellers are now expected to provide buyers with a

² See Leo Bearman, Jr., *Caveat Emptor in the Sales of Realty—Recent Assaults Upon the Rule*, 14 VAND. L. REV. 540, 571-72 (1961) (describing five theories of recovery for disappointed homebuyers in addition to implied warranty). Lord Cairns articulated the principle in *Peek v. Gurney*, 6 L.R- E. & I. App. 377, 403 (1873) ("Mere nondisclosure of material facts, however morally censurable . . . would, in my opinion form no ground for an action in the nature of . . . misrepresentation.").

³ See *Kramer v. Musser*, 136 P.2d 74, 76-77 (Cal. Ct. App. 1943).

⁴ See *Herzog v. Capital Co.*, 164 P.2d 8, 10 (Cal. 1945).

⁵ Gretchen D. Coles, *The Pennsylvania Real Estate Licensing Act: The "Miranda Warning" of Real Estate*, 107 DICKINSON L. REV. 119, 119 (2002) (quoting Deborah L. Wood, *Nailing it Down, How a Broker Can Build a New Construction Deal*, CHI. SUN-TIMES, Apr. 5, 1996 at 1, available at 1996 WL 6739332).

⁶ See *Swinton v. Whitinsville Sav. Bank*, 42 N.E.2d 808, 808-09 (Mass. 1942).

⁷ *Id.*

⁸ Alabama, Montana, Massachusetts, and Utah are the only jurisdictions not requiring sellers to disclose known material latent relied-upon defects as far as I have been able to

detailed account of known material defects. This requirement is a statutory norm in about two-thirds of the states⁹ and is an accepted practice of real estate sales agents nationwide.¹⁰ Silence is no longer golden. In fact,

determine. However, according to David Johnson, an attorney for the Utah Association of REALTORS®, there is a noticeable decline in Utah in the strict enforcement of *caveat emptor*—courts are increasingly looking at the duty of sellers to disclose their knowledge of latent, material defects. Telephone Interview by Robert Cooper, Research Assistant to Professor George Lefcoe and 2004 graduate of the University of Southern California Law School, with David Johnson, Counsel to the Utah Association of REALTORS® (July 18, 2003). In a Massachusetts case, sellers repaired a large crack in the basement slab and later observed more cracks in foundation walls. The sellers said nothing to the buyers about the repairs or new cracks in the wall. The buyers unsuccessfully sued on a theory of fraud in the inducement because sellers in Massachusetts have no obligation to disclose latent defects. *See Solomon v. Birger*, 477 N.E.2d 137 (Mass. App. Ct. 1985). In recent years, New York, Indiana, and Minnesota, formerly *caveat emptor* states, have now enacted seller disclosure statutes.

⁹ See ALASKA STAT. §§ 34.70.010-.200 (Michie 2001); CAL. CIV. CODE §§ 1102 - 1102.15, 1103 (West Supp. 2004); CONN. GEN. STAT. ANN. §§ 20-327b to -327f (West 2003 & Supp. 2004); DEL. CODE ANN. tit. 6, §§ 2570 - 2578 (1999); D.C. CODE ANN. §§ 42-1301 to -1311 (2001); HAW. REV. STAT. ANN. §§ 508D-1 to -20 (Michie 2002); IDAHO CODE §§ 55-2501 to -2512 (Michie 2003); 765 ILL. COMP. STAT. ANN. §§ 77/1 to 77/99 (West 2001); IND. CODE ANN. §§ 32-21-5-1 to -13 (Michie 1996); IOWA CODE ANN. §§ 558A.1-.8 (West Supp. 2004); KY. REV. STAT. ANN. § 324.360 (Michie 2001); LA. REV. STAT. ANN. § 3195 (West Supp. 2004); ME. REV. STAT. ANN. tit. 33, §§ 171-179 (West Supp. 2003); MD. CODE ANN., REAL PROP. § 10-702 (2003); MICH. COMP. LAWS ANN. §§ 565.951-.966 (West Supp. 2003); MINN. STAT. ANN. §§ 513.51-.60 (West Supp. 2004); MISS. CODE ANN. §§ 89-1-501 to -523 (1999 & Supp. 2003); MONT. CODE ANN. § 75-3-606 (2001) (requiring seller disclose only radon testing); NEB. REV. STAT. ANN. §§ 76-2, 120 (Michie 1996 & Supp. 2002); NEV. REV. STAT. ANN. §§ 113.120 -.150 (Michie 2004) (requiring disclosure only of private water supply and sewage disposal); N.H. REV. STAT. ANN. § 477:4-c (Supp. 2003); N.Y. REAL PROP. LAW §§ 460 - 467 (McKinney Supp. 2004); N.C. GEN. STAT. §§ 47E-1 to -10 (1999); OHIO REV. CODE ANN. § 5302.30 (Anderson Supp. 2002); OKLA. STAT. ANN. tit. 60, §§ 831-839 (West Supp. 2004); OR. REV. STAT. §§ 105.465-.490 (2003); PA. STAT. ANN. tit. 68, §§ 7301-7315 (West Supp. 2003); R.I. GEN. LAWS §§ 5-20.8-1 to -11 (1999 & Supp. 2003); S.C. CODE ANN. §§ 27-50-10 to -110 (Supp. 2003); S.D. CODIFIED LAWS §§ 43-4-37 to -44 (Michie 1997); TENN. CODE ANN. §§ 66-5-201 to -210 (Supp. 2003); TEX. PROP. CODE ANN. § 5.008 (Vernon 2004); VA. CODE ANN. §§ 55-517 to -525 (Michie 2003); WASH. REV. CODE ANN. §§ 64.06.005-.900 (West Supp. 2004); WIS. STAT. ANN. §§ 709.01 -.08 (West 2001).

¹⁰ State licensing laws differentiate between agents or salespersons and brokers, and usually require less exacting standards for salespersons and impose a process by which salespersons may become brokers. *See* CAL. CIV. CODE § 2079.13(a) (West 1998). To obtain a broker's license, the licensee must have been either a salesperson for four years or an attorney. *See id.* By statute, the term agent means broker. *See id.* In this Article, the terms agent, salesperson, and broker are used interchangeably. The term "REALTOR®" (always capitalized) is a registered mark that identifies and may be used only by real estate

silence can become extremely costly to unduly laconic sellers and their brokers.

This Article recounts the common law evolution from *caveat emptor* to "seller tell all" and explains why the courts never imposed upon sellers of used housing the implied warranties required of homebuilders. The Article also explains how, incident to the movement away from *caveat emptor*, some courts began holding brokers liable for seller errors and omissions that the courts believed brokers, as licensed professionals, should have detected and disclosed to prospective buyers.

Eventually, to keep afloat of the rising tide of consumer expectations and reduce their own exposure to legal liability, brokers endorsed the idea that sellers be given no practical choice but to fill out detailed property condition disclosure forms, which brokers would then transmit to prospective buyers.

The final section of this Article addresses some key questions that brokers needed to answer in the course of establishing seller disclosure as the norm: (1) Should property condition disclosure forms be embedded in state statutes, promulgated by state regulatory agencies, or issued by local Realtors Associations? (2) Should statutes mandate seller compliance or should compliance be voluntary, implemented through language in broker-drafted listing and residential purchase agreements obligating sellers to make full disclosure? (3) What topics should disclosure forms cover? (4) Should forms be extensive or abbreviated? (5) Should sellers be excused from being required to complete disclosure forms if they pay for professional physical inspections of their properties? (6) Should sellers be able to avoid disclosure through disclaimers and waivers? (7) Should sellers be required to disclose the existence of area-wide natural and man-made hazards, even if they would need to pay firms to gather this information for the benefit of prospective buyers?

professionals who are members of the National Association of REALTORS®, the nation's largest professional association consisting of over 760,000 real estate professionals, and who subscribe to its code of ethics. The term "Realtor," as used in this Article, refers to any real estate professional or organization that is a REALTOR®-member of the the National Association of REALTORS® ("NAR"). All other generic references to real estate professionals are expressed as "agent," "salesperson," or "broker."

II. FROM *CAVEAT EMPTOR* TO FULL DISCLOSURE FOR USED HOME BUYERS

A. The Justification for *Caveat Emptor*

When sellers had no disclosure obligations, they were protected from lawsuits by the mantra *caveat emptor*—let the buyer beware. The policy behind the norm can be distilled from the complete maxim: *caveat emptor, qui ignorare non debuit quod jus alienum emit*—“let a purchaser, who ought not to be ignorant of the amount and nature of the interest which he is about to buy, exercise proper caution.”¹¹ Between buyer and seller, the earlier rule burdened the buyer with evaluating the physical condition of the acquired property. True, the seller might know more about the property’s covert shortcomings, but being human, the sellers might have learned to live with problems that buyers might find unacceptable, they could forget incidents that occurred years earlier, or they could even decide not to mention conditions that might jeopardize a sale or force a price reduction.¹²

The rule of *caveat emptor* presumes that the buyer is in a better position than the seller to ascertain whether the condition of the property fully satisfies the buyer’s particular needs, tastes, and plans. The “due diligence” of a buyer hoping to reside in the residence without making major renovations will differ significantly from that of a buyer intending to demolish the house and build anew. The former will need a careful home inspection, while the latter should look for an architect and general contractor to review local zoning and building codes, lot dimensions, soil characteristics, and other matters pertaining to new construction.

B. Disclosure of Known Material Latent Defects Not Readily Apparent to the Buyer

Strict adherence to *caveat emptor* left buyers vulnerable to latent defects, even those known to the seller. To correct this inequity and

¹¹ HERBERT BROOM, *LEGAL MAXIMS* *769.

¹² See Florrie Young Roberts, *Disclosure Duties in Real Estate Sales and Attempts to Reallocate the Risk*, 34 CONN. L. REV. 1, 40 (2001):

Because a seller of a house, by virtue of living in the house, has far greater knowledge of any defects than would a potential buyer (even a potential buyer who did lengthy inspections), most often the seller is the cheapest cost avoider.

The seller can most cheaply avoid the loss by either fixing the problem or notifying the buyer that the problem exists.

reconcile the doctrine of *caveat emptor* with the rising tide of consumer protection law, from the 1960s onward, courts began conditioning the application of the doctrine by requiring sellers to disclose known material latent defects not known or readily apparent to the buyer.¹³

While property condition disclosure is now a statutory requirement in two-thirds of states, the common law remains important, and not just in the states without disclosure laws. For the most part, seller disclosure statutes have been drafted to complement, but not to modify or otherwise interfere with, the evolving common law of seller disclosure.¹⁴ Sellers remain obligated to disclose known material latent defects (as defined by courts over time) not readily observable to buyers.

Each of these elements—*known*, *material*, *latent*, and *reliance*—can give rise to factual disputes.¹⁵ For this reason, sellers are rarely able to obtain early dismissal of buyers' suits based on sellers' disclosure failures. Just as in suits predicated on fraud or negligent misrepresentation,¹⁶ these fact-intensive contests are seldom subject to dismissal by demurrer, motion to dismiss, or motion for summary judgment. Buyers also must be prepared to underwrite their participation in this expensive process, as they have the burden of proof on each element.

1. Known

Sellers are liable only for failing to disclose material defects actually and demonstrably known to them. With a few exceptions, noted in the last

¹³ In Alabama, home sellers need only disclose known material latent defects affecting health and safety. See Bowdy J. Brown, *The Doctrine of Caveat Emptor and the Duty to Disclose Material Defects and Other Conditions in the Sale of Single Family Residential Real Estate: Defining the Home Buyer's Legal Rights*, 61 ALA. LAW. 122, 122 (2000).

¹⁴ The New York statute, for instance, specifically preserves "any existing legal cause of action or remedy at law, in statute or equity." N.Y. REAL PROP. LAW § 467. "This article does not limit any other remedy available to the purchaser under law." S.C. CODE ANN. § 27-50-50 (C). "The specification of items for disclosure in this article does not limit or abridge any obligation for disclosure created by any other provision of law or which may exist in order to avoid fraud, misrepresentation, or deceit in the transfer transaction." CAL. CIV. CODE § 1102.8.

¹⁵ See Richard M. Jones, Comment, *Risk Allocation and the Sale of Defective Used Housing in Ohio—Should Silence Be Golden?*, 20 CAP. U. L. REV. 215, 222 (1991) ("[O]nly a clairvoyant vendor would be certain as to when he must disclose a particular fact. . . . Uncertainty exists as to when a condition is latent, when it is material, and when a [buyer] is justified in relying on a seller's nondisclosure.").

¹⁶ See Dennison v. Koba, 621 N.E.2d 734, 737-38 (Ohio Ct. App. 1993); Ferguson v. Cussins, 713 S.W.2d 5, 6 (Ky. Ct. App. 1986).

section of this Article, sellers are held accountable only for actual knowledge, not for what they should have known or could have hired an expert to discover.¹⁷ They have no duty to investigate matters in order to answer questions raised by buyers or posed in state-mandated questionnaires.¹⁸

The seller's denial of knowledge is not conclusive. Even if the seller emphatically denies knowledge, buyers can impute knowledge to the seller through circumstantial evidence,¹⁹ though this is often difficult.²⁰

Suppose when signing a purchase and sale agreement, a seller claims

¹⁷ For this reason, the Utah Association of Realtors recently revised its property condition disclosure form to facilitate sellers' telling what they know and not warranting the condition of the property being sold. For instance, on the previous form, the seller was to indicate whether the various appliances were "working" or "not working." The new form asks whether the seller is aware of any past or present problems with any of them. See UTAH ASS'N OF REALTORS®, SELLER'S PROPERTY DISCLOSURE form (2000, as revised in 2003) (on file with author).

¹⁸ See *San Diego Hospice v. San Diego*, 37 Cal. Rptr. 2d 501, 506 (Ct. App. 1995) (holding that the seller had no duty to disclose an underground storage tank of which seller was unaware, and the buyer must prove seller's actual knowledge). An important exception, California's Natural Hazard Disclosure Law, which requires sellers to inspect maps to determine if their properties are located within certain "natural hazard" zones, is described in the last section of this Article.

¹⁹ See *Colgan v. Washington Realty Co.*, 879 S.W.2d 686, 688 (Mo. Ct. App. 1994). In *Colgan*, the seller admitted only minor water intrusion, but shortly after closing, the garage roof collapsed in heavy rain and damaged the buyer's car. Despite the seller's denial of knowledge, the buyer established by circumstantial evidence that seller could not have been ignorant of the type of water intrusion manifested by the roof collapse. *But see Davis v. Kempfer*, No. 14-95-31, 1996 WL 170376, at *3 (Ohio Ct. App. Apr. 10, 1996). The buyers in *Davis* found that slab floors had sunk because of a foundation defect, but they found out only after closing when they hired a civil structural engineer to drill holes through the concrete floor slab. The court deemed the allegations that the seller had replaced carpet, installed baseboards, and arranged furniture to hide the defect insufficient proof that the seller knowingly concealed any material fact because they "could produce no witnesses to support" their claims of the seller's knowledge. *Id.*

²⁰ See, e.g., *Brasier v. Sparks*, 22 Cal. Rptr. 2d 1 (Ct. App. 1993). In *Brasier*, the buyer sought a building permit during escrow to construct a third mobile home on the site, which already contained two mobile homes. Two days before closing, the building department informed him, but not the sellers, of serious code violations. The sellers, in completing the statutory transfer disclosure statement, answered "no" to the question asking if they were aware of any work done without the requisite permits. The buyer closed anyway and later sought compensation from the sellers to correct the code violations. The sellers refused to pay. Because the buyer was unable to establish that the sellers had known of the code violations, the buyer had no recourse against them. Sellers' attorneys often cite this case for the proposition that sellers' statements are not representations of fact concerning the condition of the property but are only indications of what they know about it. *See id.*

the roof is sound and leak-free. The seller sees no reason to disclose past roof leaks that she believes have been repaired²¹ with the damaged walls and ceilings plastered and painted. Sixty days after the closing, the buyer gets drenched, is furious with the seller, and is certain that the seller intentionally concealed evidence of prior water damage. The buyer's gut feelings will not suffice. The buyer must demonstrate that at the time the seller pronounced the roof to be in good shape, the seller knew that the water intrusion problem had not been solved.²²

2. Material

Only material defects count, yet few claims are dismissed for want of materiality, perhaps because most buyers do not sue until faced with substantial losses. Materiality has been measured in various ways: (1) whether the buyer, if fully informed, would have purchased the property;²³ (2) whether a reasonable buyer would not have purchased the property; (3) whether the property is less desirable; (4) whether the price would have been substantially lower;²⁴ or (5) whether reasonable persons

²¹ See Vasilovich v. Blaney, No. B141819, 2002 WL 287788, at *1 (Cal. Ct. App. Feb. 27, 2002) (holding that vendors did not need to disclose roof leaks they reasonably believed they had cured). See also Barnhouse v. City of Pinole, 183 Cal. Rptr. 881, 892 (1982) (holding that vendors should have disclosed a landslide repair because soil instability is likely to recur).

²² See Jacobs v. Racevskis, 663 N.E.2d 653, 656-57 (Ohio Ct. App. 1995):

Racevskis claims that the various actions he took to correct defects in this home were taken solely for the purpose of repairing and remedying those existing problems, not for the purpose of misleading or deceiving anyone, one of the necessary elements of a fraudulent concealment claim. Jacobs claims, on the other hand, that Racevskis's actions, such as painting the ceiling tiles and repairing the floor, were motivated by a purpose to conceal existing defects in this home from any potential buyer. Thus, the pivotal question here is one of Racevskis's purpose or intent, a material issue of fact.

²³ See Weintraub v. Krobatsch, 317 A.2d 68, 74 (N.J. 1974):

Minor conditions which ordinary sellers and purchasers would reasonably disregard as of little or no materiality in the transaction would clearly not call for judicial intervention. While the described condition may not have been quite as major as in the termite cases which were concerned with structural impairments, to the purchasers here it apparently was of such magnitude and was so repulsive as to cause them to rescind immediately though they had earlier indicated readiness that there be adjustment at closing for damage resulting from a fire which occurred after the contract was signed. We are not prepared at this time to say that on their showing they acted either unreasonably or without equitable justification.

²⁴ See Billian v. Mobil Corp., 710 So. 2d 984, 987 (Fla. Dist. Ct. App. 1998):

would attach importance to the omitted fact in determining their course of conduct in the transaction.²⁵

One of the leading cases delimiting the outer boundary of “materiality” was widely published: *Reed v. King*.²⁶ The buyer, an elderly woman, learned after taking title that ten years earlier the home had been the site of a grisly axe murder of a mother and her four children. She sought rescission, a claim the trial court summarily dismissed. On appeal, the buyer won a reversal of the trial court’s dismissal and was given the chance to prove on remand that the fact that the house was the scene of a murder depressed the home’s market value. Subsequently, many states enacted statutes declaring that psychological impacts are not material facts, hoping to free sellers and brokers of any duty to disclose the untimely deaths or illnesses of previous occupants.²⁷

3. Latent

Expecting a seller to detail every blemish in an older home is unrealistic and wasteful. The common law rule makes sellers responsible for

As crafted by the supreme court, the materiality of a fact is to be determined objectively by focusing on the relationship between the undisclosed fact and the value of the property. To be actionable, an undisclosed fact must materially affect the value of the property. Under the Billians’ approach, the materiality of a non-disclosure would, in part, be determined subjectively, by measuring how disclosure would have affected their personal decision to purchase. Imposition of this standard would represent a departure from [Florida law].

²⁵ See *Reed v. King*, 193 Cal. Rptr. 130, 132 (Ct. App. 1983). In Ohio, sellers are only bound to disclose “material facts of a serious and dangerous condition.” See also *Klott v. Assoc. Real Estate*, 322 N.E.2d 690, 693 (1974) (holding that a seller’s failure to disclose that the property’s water supply was from a well, not the city, did not state a cause of action for nondisclosure of a material latent defect).

²⁶ See 193 Cal. Rptr. at 132.

²⁷ See Ronald Benton Brown & Thomas H. Thurlow III, *Buyers Beware: Statutes Shield Real Estate Brokers and Sellers Who Do Not Disclose That Properties Are Psychologically Tainted*, 49 OKLA. L. REV. 625, 626-28 (1996); Paula C. Murray, *AIDS, Ghosts, Murder: Must Real Estate Brokers and Sellers Disclose?*, 27 WAKE FOREST L. REV. 689, 708 (1992) (“A ‘defect’ must be defined by focusing on the property’s physical condition, not a buyer’s unusual sensitivities and prejudices. . . . The fear and prejudice of some buyers should not be allowed to influence the market unilaterally.”); Daniel M. Warner, *Caveat Spiritus: A Jurisprudential Reflection Upon the Law of Haunted Houses and Ghosts*, 28 VAL. U. L. REV. 207, 240 (1993) (“Psychologically impacted real estate evaluation is irrational and harmful, and it should be legally unacceptable.”). But see HOUSTON ASSOC. OF REALTORS SELLER’S DISCLOSURE NOTICE (2002) (on file with author) (“Death on the Property other than death caused by: natural causes, suicide, or accident unrelated to the Property’s condition.”).

disclosing only latent defects; buyers are presumed to notice patent defects on their own. There is no reason to require the seller to notify the buyer of patent defects that any observant buyer could have noticed.

While contracting parties are never required to disclose everything they know about the subject property, scholars of law and economics distinguish between information casually acquired and information obtained through deliberate and costly research.²⁸ To learn of latent defects, most buyers would need to pay for professional assistance. Sellers learn of such defects in the normal course of homeownership without any special investment in the acquisition of the information. Requiring sellers to share this information with prospective buyers saves buyers money.

Although courts recognize that the price buyers are willing to pay often depends on their assumptions about the condition of the property,²⁹ courts do not determine whether a condition is patent or latent based on evidence of whether the purchase price or other deal terms accounted for the condition.³⁰ Instead, the courts draw distinctions rooted in their common sense assumptions of what buyers would observe or overlook. For instance, the purchaser of a four-plex with no on-site parking was presumed to have noticed the lack of parking when he visited the site.³¹

²⁸ See Anthony T. Kronman, *Mistake, Disclosure, Information, and the Law of Contracts*, 7 J. LEGAL STUD. 1, 33 (1978). A seller is required to disclose to the buyer known material latent defects, but a buyer is not required to disclose to the seller the results of its demographic and market studies indicating the "highest and best" use of the subject property. Requiring buyer disclosure would inhibit socially useful information gathering. Seller disclosure has no social costs.

²⁹ See *Newhall Land & Farming Co. v. Superior Court*, 23 Cal. Rptr. 2d 377, 382 (Ct. App. 1993):

[I]n *Pinole Point Properties*, the plaintiff knew of the existence of the contamination before acquiring the property. Thus, the damage to the property caused by the defendant's use of the waste disposal pond could be factored into the terms of the purchase. In contrast here, Mobil and Amerada did not disclose the existence of the contamination when the property was sold. Consequently, the effect of Mobil and Amerada's unlawful discharge of hazardous materials into the soil could not be considered when the purchase was negotiated.

³⁰ However, when the seller or landlord is bound by an implied warranty of habitability, fitness for use, or workmanship, courts may take the purchase price or rent level as evidence of whether the seller or landlord met their obligation. See, e.g., *Timber Ridge Town House v. Dietz*, 338 A.2d 21 (N.J. Super. Ct. Law Div. 1975); *Tobin v. Paparone Constr. Co.*, 349 A.2d 574 (N.J. Super. Ct. Law Div. 1975).

³¹ See *Matthews v. Kinkaid*, 746 P.2d 470, 472 (Alaska 1987). In *Matthews*, the buyer claimed he had been told by the seller and broker that his tenants could park next door or on the street, twenty-two out of twenty-four hours a day. Shortly after he purchased the

In practice, courts differ on whether certain types of defects are patent or latent. For example, courts are divided on issues of whether buyers should notice termite infestation outside of the normal termite swarming season³² or water intrusion into crawl spaces located beneath the house.³³

4. Reliance

Whether a reasonable purchaser would rely on any particular statement made by the seller or the seller's agent may become a contested question of fact.³⁴ Courts have forgiven some sellers and brokers for some sales puffing (the kind of promotional chatter most buyers would ignore).³⁵ Buyers can rely on statements of fact made by sellers or brokers, but not

building, the city banned on-street parking, and his tenants had no right to park on the adjoining site, which contained a six-unit building. The court remarked:

Any person who viewed the property could see that there was no parking area on Matthews' lot. Although there was a parking area in front of the multi-unit dwelling next door, it was too small to accommodate the tenants of both buildings. Further, the area was separated from Matthews' lot by a chain link fence, and therefore was not easily mistaken for Matthews' property.

Id.

³² For the conflicting case outcomes, see E. T. Tsai, Annotation, *Duty of Vendor of Real Estate to Give Purchaser Information as to Termite Infestation*, 22 A.L.R.3d 972 (1968).

³³ See *Bennett v. Cell-Pest Control, Inc.*, 701 So. 2d 1122, 1124 (Ala. 1997) (deeming rotted floor joists visible only by looking just above crawl space to be a patent defect); *Lee v. C.D.E. Home Inspection Co.*, 2002 WL 1938248, at *5 (Ohio Ct. App. Aug. 22, 2002) (deeming crawl space inaccessible and beyond the scope of home inspector's reasonable search because water intrusion could not be detected without entering the space).

³⁴ See *Gouveia v. Citicorp Person-to-Person Fin. Ctr., Inc.*, 686 P.2d 262, 268 (N.M. Ct. App. 1984):

There is, at best, an issue of material fact as to the Gouveias' reliance on the "All Top Shape" representation on the record which precludes the grant of summary judgment. We cannot say, on the record before us, that no reasonable purchaser would rely on such a representation under these facts.

³⁵ See Cullen Goretzke, Comment, *The Resurgence of Caveat Emptor: Puffery Undermines the Pro-Consumer Trend in Wisconsin's Misrepresentation Doctrine*, 2003 WIS. L. REV. 171, 173. Puffery is a representation ordinary customers do not take seriously.

It is in the nuanced distinction between actual reliance and justifiable reliance that caveat emptor survives and where the hypothetical nature of puffery is exposed. Individuals, who, in fact, rely on false representations to their detriment, may not prevail on a misrepresentation claim if the court holds that the representations are such that ordinary individuals would not take them seriously; in other words they are puffery.

Id.

on statements of opinion.³⁶

Even with proof that a seller lied about a material fact, a buyer is not assured of prevailing if the lie was transparent. If a buyer sees clues sufficient to indicate potential sources of trouble, a homebuyer's exercise of due diligence may require hiring professional inspectors³⁷ and making inquiries to local officials regarding zoning, building code compliance, and environmental conditions.³⁸ Lackadaisical buyers risk being burdened with seriously defective houses or parcels of land on which they cannot build.³⁹

³⁶ See *Cornelius v. Austin*, 542 So. 2d 1220, 1223 (Ala. 1989). In *Cornelius*, the buyers asked the sellers if there were any problems with the house and the seller replied no. The Alabama Supreme Court held that such a statement constituted an opinion, not a representation of fact. See also *Williamson v. Realty Champion*, 551 So. 2d 1000, 1002 (Ala. 1989) ("With regard to Gunter's statement that the house was 'very well built,' we have held that general statements such as this are not evidence of fraud because they are 'statements of the seller's opinion and not of fact.'") (quoting *Ray v. Montgomery*, 399 So. 2d 230, 232 (Ala. 1980)).

³⁷ See *McClain v. Papka*, 108 S.W.3d 48, 52 (Mo. Ct. App. 2003) ("A plaintiff asserting fraud must show that the undisclosed information was beyond his or her reasonable reach and not discoverable in the exercise of reasonable diligence."). See cases collected at Robert M. Washburn, *Residential Real Estate Condition Disclosure Legislation*, 44 DE PAUL L. REV. 381, 405 (1995).

³⁸ See *Clouse v. Gordon*, 445 S.E. 2d 428, 433 (N.C. Ct. App. 1994). In *Clouse*, the property was located in a federally designated special flood hazard zone, but the buyers never proved that the sellers knew this fact. Even if the buyers had shown the sellers' knowledge, "[I]t is the policy of the courts not to encourage negligence and inattention to one's own interest. The purchaser is under some duty to insure that their interests are preserved." *Id.* (citations omitted). In *Sweat v. Hollister*, 43 Cal. Rptr. 2d 399 (Ct. App. 1995), the broker told the buyers the property was in a flood plain. After the sale, the buyers learned that the municipal code prevented them from altering or enlarging their property in the event of partial destruction and restricted their ability to make other improvements. The court noted that the buyers could have determined the effect of local ordinances on the property just as easily as the broker. Thus, there was no justification for holding the broker accountable to the purchasers. See *id.* at 401. See also *Pakrul v. Barnes*, 631 S.W.2d 436, 438 (Tenn. Ct. App. 1981) (finding that a buyer with notice of possible zoning problems had the opportunity to determine from local officials whether his intended use complied and could not justifiably rely on broker's opinion that the property was properly zoned for his use). But see *Asleson v. W. Branch Land Co.*, 311 N.W.2d 533, 542-43 (N.D. 1981) (holding that where the seller listed property as being zoned for thirty-five apartment units when it was only zoned for thirty, the buyers were entitled to rely on the seller's misrepresentation because they were not relying irrationally, preposterously, or in bad faith).

³⁹ See, e.g., *Soursby v. Hawkins*, 763 P.2d 725 (Or. 1988). In *Soursby*, the buyers sought rescission after closing when they learned that the vacant parcel they had purchased

Buyers who learn about defects from their own inspectors cannot claim to have justifiably relied on the seller's misleading statements or failure to disclose.⁴⁰ Courts instruct juries that a buyer who hires a professional inspector is presumed to depend upon the inspector's conclusions and not upon contradictory, casual statements made by the seller.⁴¹ Even when a buyer's professional inspector negligently overlooks a serious property defect, some courts have denied buyers recourse against the sellers or brokers.⁴² Other courts do not allow the negligence of the

as a home site could not be used for residential purposes without expensive road improvements. The listing broker had innocently misrepresented that the lot was properly zoned for residential use. The court found that whether the buyers' reliance had been reasonable was a question of fact.

⁴⁰ See Aranki v. RKP Invs., Inc., 979 P.2d 534, 537 (Ariz. Ct. App. 1999) ("[The buyer's] only evidence calls their own reliance into question: plaintiffs hired a professional inspection service for the purpose of revealing defects, and this report identified at least some of the problems that form the basis of plaintiffs' damages claim."); Mobley v. Copeland, 828 S.W.2d 717, 726 (Mo. Ct. App. 1992) ("When a party makes an independent investigation he is presumed to have relied on what he learned from that investigation and may not claim that he relied on a misrepresentation."); Camden Mach. & Tool v. Cascade Co., 870 S.W.2d 304, 311 (Tex. App. 1993) (holding that a buyer had no right to recover against a listing agent's reckless representation that a crack in the building's foundation was of minor significance because he had obtained reliable opinions and estimates of repair costs on his own from several contractors and a facilities engineer); Conell v. Coldwell Banker Premier Real Estate, Inc., 512 N.W.2d 239, 242 (Wis. Ct. App. 1994) (finding that a buyers' home inspection clearly disclosed a basement water problem even if a seller's disclosure was not sufficiently clear).

⁴¹ CAL. JURY INSTR.—CIV.12.53 (West 2004):

If plaintiff independently investigates the subject matter of the alleged false [representation] [or] [promise] and the decision to engage in the transaction is the result of [his] [or] [her] independent investigation and not [his] [or] [her] reliance upon the [representation] [or] [promise], [he] [or] [she] is not entitled to recover.

⁴² See *id.* See also Brickman v. Scheitlin, 58 Fed. Appx. 282, 283 (9th Cir. 2003) (not selected for publication in Federal Reporter) (holding it is a question of fact whether a home buyer, who obtained a property inspection report prior to purchase, knew or should have known of the existence of problems in the home's sewer line and drainage); Clouse, 445 S.E.2d at 433 (finding the buyers had no recourse against the sellers when the buyers' surveyor erred by concluding the property was not in a flood plain, representing that he had consulted the Federal Emergency Management Agency Flood map and determined the property was not in a special flood hazard zone). But see Lindberg v. Roseth, 46 P.3d 518, 524 (Idaho 2002):

An inspection of the property, by itself, does not preclude buyers from bringing an action for fraud. If any latent defects that are not discoverable upon a reasonable inspection exist, the buyer who has made an inspection and did not discover such defects can still recover if the seller fraudulently failed to disclose

buyer's inspector to excuse the seller's dishonesty.⁴³ An intermediate position would allow a finding of contributory negligence for the buyer's failure to make an adequate inspection.

5. An "Undisclosed Defect" Hypothetical

To appreciate how these elements often render dispute outcomes unpredictable, consider the case of the buyer who purchased a log house that leaked badly during rainstorms.⁴⁴ As the buyers wandered through the house, inspecting it for themselves, they noticed a black tarp on the floor, mildew stains on the ceiling and walls, and a log broken off from an exterior corner. The seller attributed the problem to the roof not having been extended far enough to cover the log. The buyers never hired a professional home inspector. After closing and taking possession, the buyers discovered the leakage problem was very serious. Neighboring owners pointed out that the logs on the buyers' newly acquired home had been installed upside down, preventing the log surface from properly shedding water. During heavy rains, water collected between the logs,

or misrepresented the existence of such defects.

⁴³ See *Robinson v. Grossman*, 67 Cal. Rptr. 2d 380, 382 (Ct. App. 1997). In *Robinson*, the buyer's excavation for a pool collapsed shortly after closing as a result of a landslide and creeping soils. The buyers sued the broker, claiming that the broker had an obligation to verify the seller's claim that stucco cracks were merely cosmetic. But the broker had carefully noted the existence of the cracks and urged the buyer to obtain a geotechnical inspection. Instead of taking this advice, the buyer relied on a home inspector who never detected the soils problem. *See id.* The court held that the broker had not done anything wrong, and the buyer should have taken the broker's good advice to investigate the soils before purchasing the home. *See id.* at 385. The broker had no duty to verify the representations made by the seller. *See id.* at 387. *See also Besett v. Basnett*, 389 So. 2d 995, 997 (Fla. 1980) (finding that seller fraud trumps buyer negligence when the buyer relies on a seller's reasonably convincing misrepresentation); Ron Rossi, *Sellers' Dishonesty in Los Gatos Deal Costs Them in Court*, SAN JOSE MERCURY NEWS, Feb. 15, 2003 available at <http://www.rhrc.net>. In a binding arbitration case, the sellers claimed that no noise emanated from a commercial building that backed up to the home's backyard and that it was only a retail auto parts store. The sellers knew it was a noisy auto repair shop with five bays and had persuaded operators to keep the front doors closed during the time they were marketing their home. The arbitrator, a retired Superior Court judge, granted the buyers' demand for rescission, concluding that the buyers had reasonably relied on the sellers' fraudulent misrepresentation even though the buyers could have visited the commercial building and seen for themselves the nature of the business being conducted there. *See id.*

⁴⁴ See *White v. Huett*, No. COA00-1328, 2002 WL 1900323, at *1 (N.C. Ct. App. Aug. 20, 2002).

damaged the interior, and rotted the wood.⁴⁵

As in so many undisclosed defect cases, this one easily could have been decided the other way. The buyers were not able to demonstrate conclusively that the seller had actually known the true cause of the problem. The court could have ascribed knowledge to the seller despite her denial if the buyers had shown that the seller discussed the inverted log situation with her more observant neighbors.⁴⁶

The buyers' failure to have the house professionally inspected weakened their case and evidenced a lack of due diligence on their part. But by not hiring an inspector, the buyers preserved their claim of reliance on the seller's erroneous but plausible explanation for the water damage.

Whether the defect was patent or latent also was contested. By comparing the placement of the logs with those in neighboring homes, the buyers could have seen the differences for themselves. Buyers, after all, are solely responsible for items known to them or within their diligent attention.⁴⁷ Conversely, a trier of fact could have concluded that the problem was subtle enough to be beyond the reasonable observation of the typical buyer.

Examples like this demonstrate the importance of warranties and representations and the world of difference between these and disclosure obligations. When it comes to the sale of "used" housing by ordinary homeowners—about eighty-five percent of all home sales⁴⁸—amateur sellers are not held liable for impliedly warranting the condition of the property sold.⁴⁹ As long as the buyer had a chance to inspect the property beforehand, what the buyer saw was what the buyer got—unless the buyer contracted for a warranty from the seller.⁵⁰ Courts flatly refused to imply

⁴⁵ See *id.* at *2-4.

⁴⁶ See *id.* at *3-4.

⁴⁷ See, e.g., CAL. CIV. CODE § 2079.5 (West Supp. 2004).

⁴⁸ In 2000, for instance, there were 877,000 new home sales and 5,842,000 sales of existing homes. See U.S. DEPT. OF COMMERCE, STATISTICAL ABSTRACT OF THE UNITED STATES: THE NATIONAL DATA BOOK 598, 600 (21st ed. 2001).

⁴⁹ See *Copland v. Nathaniel*, 624 N.Y.S.2d 514, 522 (Sup. Ct. 1995) ("There is no implied warranty of habitability in the sale of a previously owned home.").

⁵⁰ See, e.g., *Barnard v. Kellogg*, 77 U.S. 383, 388 (1870):

No principle of the common law has been better established, or more often affirmed, both in this country and in England, than that in sales of personal property, in the absence of express warranty, where the buyer has an opportunity to inspect the commodity, and the seller is guilty of no fraud, and is neither the manufacturer nor grower of the article he sells, the maxim of *caveat emptor* applies. Such a rule, requiring the purchaser to take care of his own interests, has

warranties for fear of giving buyers more than the benefit of their bargains⁵¹ and opening courtroom doors to endless litigation. Had the seller of the leaky log house warranted or represented that it was waterproof, she would have been forced to pay to cure the problem. Under a disclosure regime, she would have had a chance of escaping liability entirely—as she did in this case.

III. FROM *CAVEAT EMPTOR* TO IMPLIED WARRANTIES FOR HOMEBUILDERS

Only in the sale of newly built homes has *caveat emptor* been completely supplanted by court and legislature-imposed implied warranties of habitability and workmanship. Homebuilders are responsible for construction defects not only to their buyers but also to their buyers' buyers,⁵²

been found best adapted to the wants of trade in the business transactions of life. And there is no hardship in it, because if the purchaser distrusts his judgment he can require of the seller a warranty that the quality or condition of the goods he desires to buy corresponds with the sample exhibited. If he is satisfied without a warranty, and can inspect and declines to do it, he takes upon himself the risk that the article is merchantable.

See also Roberts, *supra* note 12, at 40 n.235 (“There may be some difference of opinion between a buyer and a seller as to what is a material defect. A defect that a buyer considers material may not be thought of as material by a seller, and, therefore, the seller will not disclose it.”).

⁵¹ See Alan M. Weinberger, *Let the Buyer Be Well Informed?—Doubting the Demise of Caveat Emptor*, 55 MD. L. REV. 387, 392 (1996):

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

⁵² See Michael A. Disabatino, Annotation, *Liability of Builder of Residence for Latent Defects Therein as Running to Subsequent Purchasers from Original Vendee*, 10 A.L.R.4th 385 (1981). The author notes the division between courts on whether to extend the benefit of implied warranties to subsequent purchasers. The annotation states:

The courts that have considered the matter have generally held that where a remote purchaser can prove actual negligence on the part of a builder vendor which results in foreseeable injury or loss to the remote purchaser, the remote purchaser should be able to recover. . . . On the other hand, courts have resisted extending an express warranty given by the builder to the original purchaser so as to permit subsequent purchasers to bring suit on the basis of contracts to which they were not parties.

Id. at 388.

subject to state-enacted statutes of repose.⁵³ By contrast, homebuyers purchasing used housing from amateur sellers receive the benefit of only those warranties they coax from their sellers or acquire from insurers.

This movement away from *caveat emptor* in real estate lagged behind a comparable movement in the law of the sale of goods by half a century. The eminent legal historian, Lawrence Friedman, reminds us that in the nineteenth century, *caveat emptor* was the legal norm for the law of the sale of goods as well as real estate.⁵⁴ Just after California gained statehood in 1850, a group of San Francisco lawyers petitioned the state legislature to embrace the civil law's pro-consumer stance. In civil law countries (and Louisiana), implied warranties were the norm, predicated on the notion that "[a] sound price requires a sound commodity."⁵⁵ The judiciary committee of the California Senate adamantly rejected this norm, characterizing it as unmanly because it coddled complaining buyers. The state senators preferred *caveat emptor*, describing it as "one of the glories of the common law, in contrast to the flabby solicitude of civil law."⁵⁶ The rule "enhanced the finality of bargains. It made it harder for parties to drag into court their harangues over warranty and quality."⁵⁷

Yet, by 1900, United States courts were abandoning *caveat emptor* in favor of implied warranties of merchantability for goods sold by description and not inspected before sale. This exception covered most manufactured goods because buyers often did not have the chance to inspect them before purchase and buyers were forced to accept form contracts without the chance to negotiate warranties. Carmakers were among the first to be held accountable in tort for product defects. Implied warranties of fitness assured buyers the right to insist upon goods being usable for the stated purposes for which they had been marketed.⁵⁸ The triumph of implied warranties in the law of sales seemed "more consonant with market

⁵³ See Martina R. Fleisher, Annotation, *Validity, As to Claim Alleging Design or Building Defects, of Statute Imposing Time Limitations upon Action Against Architect, Engineer, or Builder for Injury or Death Arising out of Defective or Unsafe Condition or Improvement to Real Property*, 2002 A.L.R.5th 21 (2002) (not released for publication); Jay M. Zitter, Annotation, *Validity and Construction of Statute Terminating Right of Action for Product-Caused Injury at Fixed Period after Manufacture, Sale, or Delivery of Product*, 30 A.L.R.5th 1 (1995).

⁵⁴ See LAWRENCE M. FRIEDMAN, A HISTORY OF AMERICAN LAW 262-66 (2d ed. 1985).

⁵⁵ *Id.* at 265 (quoting *Barnard v. Yates*, 10 S.C.L. (1 Nott & McC.) 142, 145 (S.C. 1818)).

⁵⁶ *Id.* at 265.

⁵⁷ *Id.* at 540-41.

⁵⁸ *See id.* at 540-42.

principles, because it carrie[d] out the reasonable intention of honest parties.”⁵⁹

*Schipper v. Levitt & Sons, Inc.*⁶⁰ was the landmark case applying manufacturers’ liability to the sale of newly built tract houses.⁶¹ Levitt & Sons was an easy real estate target with the precedent of automobile manufacturer’s product liability law. The company emulated the efficiency of assembly line production techniques, except that at Ford, the cars traveled along a conveyer belt as each worker performed a specialized task. At a Levitt & Sons site, each specialized trade group moved from house to house to complete its work. Although a few state courts already had rejected *caveat emptor* and implied a warranty of fitness for use in the sale of tract houses, *Schipper* started a judicial avalanche that buried *caveat emptor* for good.⁶²

Lawrence Schipper, sixteen months old at the time, was severely scalded by water from a spigot in the bathroom that flowed at 190 to 210 degrees Fahrenheit—well above the normal 140 degrees flowing from most domestic hot water taps.⁶³ The injured infant spent seventy-four days in the hospital and underwent two skin grafts.⁶⁴

All this would have been prevented if Levitt & Sons—the architect, engineer, planner, designer, builder, and contractor of the home—had followed the advice of the company that sold it the home’s boiler. Levitt had been advised to install a mixing valve to cool the water as it flowed from the boiler to the bathroom sink six feet away. The valve wholesaled for \$3.60, retailed for \$9 or \$10, and was ultimately installed after the accident by Lawrence Schipper’s dad for \$18 (for labor and materials).⁶⁵

Levitt & Sons management had decided to save the cost of the mixing valve and instead just warn homebuyers to cool the unusually hot water by always turning on the cold water spigot first. The Schippers had not heard

⁵⁹ See *id.* at 265.

⁶⁰ See 207 A.2d 314 (N.J. 1965).

⁶¹ See 12 AM. JUR. 2D *Proof of Facts* § 2 at 115 (1977) (noting that “in the area of consumer products liability, two-thirds of the courts in the US have abandoned the tort-contract labyrinth of implied warranty in favor of the doctrine of strict liability in tort.”). See also Lynn Y. McKernan, *Strict Liability Against Homebuilders for Material Latent Defects: It’s Time*, Arizona, 38 ARIZ. L. REV. 373, 391 n.91 (1998) (referencing multiple cases in which courts imposed strict liability).

⁶² See generally E. F. Roberts, *The Case of the Unwary Home Buyer: The Housing Merchant Did It*, 52 CORNELL L. Q. 835 (1967).

⁶³ See *id.* at 847.

⁶⁴ See *Schipper*, 207 A.2d at 317-18.

⁶⁵ See *id.* at 319.

this cautionary word—although at some point, the landlord had placed a written note in the bathroom warning guests of the danger.

The Schippers had leased the house for one year from the original purchaser and had no direct contract with the homebuilder—Levitt & Sons—from whom their landlord had purchased the home.⁶⁶ For this reason, their legal theory was based in tort, not contract. While the plaintiff's counsel had the heavy burden of persuading the New Jersey courts to reverse established legal doctrines, the heart-rending facts of the case lightened that burden.

Schipper embraces the same justifications as products liability law: cost spreading, risk prevention, and efficiency. Producers of defective products are in a better position than injured consumers to absorb the costs of accidents, prevent design and construction defects by developing and deploying improved products and methods, and make cost-safety trade-offs. After the *Schipper* case, Levitt & Sons' cost accountants needed to consider whether it made more sense to install mixing valves or to compensate those injured for want of mixing valves. Today, many homebuilders have learned to respond rapidly to consumer complaints of claimed defects, whether covered by warranty or not, because it is often far less costly to satisfy the buyer than to litigate.

Some lawyers worried that mandatory disclosure or “seller tell all” provisions would lead to the imposition of implied warranties upon amateur home sellers.⁶⁷ But that has not happened.⁶⁸ Disclosure statutes uniformly caution that a seller's truthful disclosure is not to be taken as a warranty of the condition of the property being sold. Similarly, disclosure forms typically proclaim, sometimes in a big, bold font: “This is not a warranty.”

Sensibly, courts have never implied a warranty of fitness or workmanship against amateur home sellers, recognizing that the product liability

⁶⁶ See *id.* at 317.

⁶⁷ See James D. Lawlor, *Seller Beware: Burden of Disclosing Defects Shifting to Sellers*, A.B.A. J., Aug. 1992, at 90 (“Some critics of mandatory disclosure fear that it exposes sellers to additional liability. Language in a disclosure document stressing that it is neither a warranty nor part of the contract between buyer and seller should minimize the risk.”).

⁶⁸ See, e.g., Lopez v. Willow Tree Homes and Commercial, Inc., No. B159212, 2003 WL 21213245 (Cal. Ct. App. May 27, 2003) (stating that seller had no liability for implied warranty after closing; buyer had no right to expect a perfect home when purchasing a thirty-two year old mobile home sold “as is” and even when buyer had complained of a dangerously loose handrail).

rationales are inapplicable to the typical home seller. Most home owners, when they sell, are not necessarily richer or better cost-spreaders than their buyers. Nor do they know more about how best to build or maintain houses, or how to shape the design and influence the design and construction decisions of homebuilders.

IV. WHY BROKERS ARE THE DRIVING FORCE BEHIND THE SELLER DISCLOSURE MOVEMENT

Politically, the driving force behind seller disclosure requirements has been NAR. NAR is the preeminent trade association to which the overwhelming majority of active residential brokers and sales persons belong.⁶⁹ In 1991, when NAR revved up its campaign for the use of property condition disclosure laws,⁷⁰ disclosure laws existed only in California and Maine. NAR's campaign has been an overwhelming success. As noted earlier, property condition disclosure forms are now required of sellers in two-thirds of the states and are widely used in the remaining states.

Some broker resistance to full disclosure norms would be understandable. Residential real estate agents are in the business of marketing and selling homes, and their compensation is contingent on sales. Brokers earn nothing for pointing out facts that kill a deal.⁷¹ Usually sales are best achieved by accentuating the positive, not by zeroing in on an exhaustive description of all the home's major hidden flaws—at least not until the

⁶⁹ NAR has over one million members organized into 1,600 local associations and boards and 54 state or territory associations. See NAT'L ASS'N OF REALTORS, 2004 FACT SHEET 1 (2004), at <http://www.realtor.org/rocms/nsflpages/aboutnar> (last visited May 5, 2004).

⁷⁰ See Note, *The Ass Atop the Castle: Competing Strategies for Using Campaign Donations to Influence Lawmaking*, 116 HARV. L. REV. 2610, 2625 (2003) ("Nationwide, the most generous corporate PAC of the 2002 cycle was that of the National Association of Realtors, which gave over \$3.6 million to candidates. The PAC was fairly bipartisan in its giving, with 47% of its donations going to Democrats and 53% to Republicans...."); News Release, National Association of Realtors, Property Disclosure by Seller Helps Everyone, NAR Says (June 24, 1991) ("At its recent Washington Mid-Year Conference, NAR adopted a policy to encourage state associations to develop and support legislation or regulation mandating property condition disclosure by the seller.") (on file with author). See also Weinberger, *supra* note 51, at 387-97 nn. 7-9.

⁷¹ See William D. LeMoult, *The Duty of Residential Real Estate Brokers and Salespersons to Disclose Property Condition to Buyers*, 70 CONN. B. J. 435, 455 (1996) (noting the inherent conflict between earning a commission on a completed sale and advising "buyers of matters which might have the effect of destroying the deal which they have been specifically commissioned to accomplish").

buyer is emotionally committed to the acquisition.⁷² Some brokers worry that meticulously honest sellers could lose buyers to less-candid or more desperate sellers.⁷³ Sometimes sellers admit property defects to their sales agents, requesting strict confidence. If the agent breaches that confidence by making full disclosure to a prospective buyer, the seller is likely to feel betrayed.

Brokers overcame these doubts partly in response to home defect litigation brought by disappointed buyers successfully targeting listing and seller brokers, along with sellers. Potential liability for what the seller fails to disclose about the condition of the property has long been a concern of the real estate brokerage profession. According to some insurance industry estimates, two-thirds of buyers' claims against sellers and brokers involve non-disclosure, and the average award in such cases has more than doubled since 1984.⁷⁴

Realtors hoped that full disclosure by sellers would cut down on defect litigation, and that buyers who were not deterred from litigating would lose their lawsuits over matters that were previously disclosed. "The buyer can't come back and say, 'You didn't tell me. . . .'"⁷⁵ In mandating honesty as the best policy, seller disclosure requirements also help to resolve the theoretical conflict between the listing broker's fiduciary duty of utmost loyalty to the seller and the listing broker's duties of due care, good faith, honesty, and fair dealing to the buyer. When brokers have been held liable for relaying misinformation supplied by sellers,

⁷² *Id.* at 455:

Simply stated, imagine trying to sell anything belonging to someone else, to whom you owe a fiduciary duty, while exposed to a corresponding duty under the law to point out every negative factor which may be of imaginable importance to the buyer, under conditions where there are no guidelines as to those that might affect the desirability or value of the property!

⁷³ See Steven W. Koslovsky, *To Disclose or Not to Disclose: An Overview of Fraudulent Nondisclosure*, 50 J. MO. B. 161, 161 (1994) ("While blanket disclosure of all facts might avoid any subsequent suits for fraudulent nondisclosure, it may also cause a client to unnecessarily disclose information which will put it at a competitive disadvantage, or even terminate a transaction.").

⁷⁴ Lawlor, *supra* note 67, at 90. The number of lawsuits against brokers increased substantially between 1987 and 2000, and the largest number of claims arose out of misrepresentations and failure to disclose property defects. See LeMoult, *supra*, note 71, at 455.

⁷⁵ Christian Murray, *Sellers, Know Thy House*, NEWSDAY, Mar. 1, 2002, available at 2002 WL 2730601 (quoting Howard Goldson, a lawyer with Goldson Nolan Associates, general counsel for the Long Island Board of Realtors, who believes the New York disclosure law "will actually reduce litigation").

disclosure laws give agents recourse against the mistaken or dishonest seller.⁷⁶ Some laws completely exonerate an agent from liability for innocently or negligently passing along inaccurate information provided by a seller.⁷⁷

Full disclosure by sellers reduces buyer claims against brokers, while a strict regime of *caveat emptor* has the opposite effect. A recent study of insurance claims against real estate salespersons in five southern states

⁷⁶ In Minnesota, where the state Realtors' boards and associations pursued enactment of a seller disclosure law, "agents were being sued for problems that sellers didn't tell them about and were paying millions to settle those lawsuits." Donna Halvorsen, *Disclosure Law: New State Law Compels Disclosure; Starting Jan. 1, Sellers Must Reveal Problems, But Buyers Still Will Have Few Remedies*, STAR TRIB., June 1, 2002 (quoting Glen Dorfman, Minnesota Realtors Association's Executive Officer), available at 2002 WL 5375981. See Clarence E. Hagglund & Britton D. Wiemer, *Caveat Realtor: The Broker's Liability for Negligent and Innocent Misrepresentations*, 20 REAL EST. L.J. 149, 165 (1991) (discussing how standard disclosure forms may help "insulate the realtor from liability for seller misrepresentations"). See also *Salahutdin v. Valley of Cal., Inc.*, 29 Cal. Rptr. 2d 463, 464 (Ct. App. 1994). In *Salahutdin*, the buyers' broker knew that the buyers desired to purchase a lot large enough to subdivide into two lots, one for their son, the other for their daughter. Because the community where the buyers were looking—Hillsborough, California—mandated half-acre minimum lot sizes, the buyers required a parcel of at least one acre. Their broker believed he had found such a parcel, relying on the listing broker's brochure describing the property as "one acre-plus." *Id.* at 465. The listing broker had, in turn, relied on the seller for the lot size information. The buyers bought the property. Ten years later, they learned the property was only .998 acres. The buyers obtained a judgment against their broker for \$175,000 to compensate for what the property would have been worth on the date of discovery had it actually been one acre. *See id.* at 466. The court held the buyers' broker liable for flaws in the property offered for sale based on the buyers' expectations. The court awarded damages to the buyers, as beneficiaries of a fiduciary relationship, on the theory of "constructive fraud," and the damages were based on the value the parcel would have had if the lot had been a full acre or larger—"benefit of the bargain" damages. Other California appellate courts have held that the proper measure of damages for breach of a fiduciary relationship involving intentional fraud should be limited to out-of-pocket damages, not the benefit of the bargain. *See, e.g., Hensley v. McSweeney*, 109 Cal. Rptr. 2d 489 (Ct. App. 2001) (awarding out-of-pocket damages); *Tennant v. Lawton*, 615 P.2d 1305 (Wash. Ct. App. 1980) (finding the broker liable, along with seller, for relaying to the buyer without independent verification of the seller's mistaken assurances concerning suitability of the property for a septic tank and awarding the buyer benefit of the bargain damages). *But see Provost v. Miller*, 473 A.2d 1162, 1163 (Vt. 1984) ("An agent can properly rely upon statements of the principal to the same extent as upon statements from any other reputable source.").

⁷⁷ Typical of the language in most seller disclosure statutes, Rhode Island's seller disclosure law specifies: "The agent is not liable for the accuracy or thoroughness of representations made by seller in the written disclosure or for deficient conditions not disclosed to the agent by the seller." R.I. GEN. LAWS § 5-20.8-2(a) (1999 & Supp. 2003).

concluded that seventy-six percent of all these suits "had something to do with the condition of the property being sold."⁷⁸ One of the five jurisdictions, Alabama, was a *caveat emptor* state. The other four—Louisiana, Kentucky, Mississippi, and Tennessee—had enacted mandatory seller disclosure laws. One of the states, Louisiana, followed the civil law and implied a warranty of fitness against all home sellers. Based on the number of licensees and average number of annual home sales, claims were far more frequent in Alabama than in Louisiana.⁷⁹ In the other three states, claim frequency fell between the Alabama and Louisiana extremes. As the authors of the study concluded: "There seems to be little question that the property condition disclosure, whether mandatory or voluntary, can reduce error and omission claims against real estate licensees."⁸⁰

As practical business people, brokers saw substantial marketing advantages accompanying seller disclosure. Some sellers, rather than having to confess to embarrassing defects, volunteered last minute improvements that made their properties more attractive and justified higher asking prices.⁸¹ Brokers also discovered that buyers were less likely to bolt from deals if weaknesses noted by home inspectors had been forthrightly described at the outset.

Most important of all, satisfaction with their purchases rose measurably among buyers who felt they had been told the truth about the property.⁸² Brokers care about customer satisfaction because satisfied buyers

⁷⁸ Leonard V. Zumpano & Ken H. Johnson, *Real Estate Broker Liability and Property Condition Disclosure*, 31 REAL EST. L. J. 285, 290 (2003).

⁷⁹ See *id.* at 289, tbl. 2.

⁸⁰ *Id.* at 299. The authors pointed out that property condition disclosure is only one factor contributing to a reduction in errors and omissions claims. Brokers must engage in ongoing risk management practices to minimize claims. See *id.* at 300.

⁸¹ NAT'L ASS'N OF REALTORS, PROPERTY CONDITION DISCLOSURE, app. D, 5 (1991) (on file with author).

⁸² Purchasers "who have been provided with a property condition disclosure form generally are more satisfied with their purchases because there are fewer surprises about the property." Brokers observed that buyers who were fully and demonstrably forewarned of defects in writing before purchasing were less likely to complain and file lawsuits. NAT'L ASS'N OF REALTORS® PROPERTY CONDITION DISCLOSURE, *supra* note 81, at 4. NAR relied upon Research Report No. 46 (Ohio State University Center for Real Estate Education and Research, 1991) prepared by Gary S. Moore, Gerald Smolen and Lawrence Conway. Professor Moore now wonders whether disclosure may have increased litigation by providing plaintiffs' lawyers with handy and convincing evidence of seller non-disclosure. Email from Gary S. Moore, Professor, University of Toledo, College of Business Administration, to George Lefcoe, Professor of Law, University of Southern California Law School (Dec. 19, 2003).

may refer their friends to the broker, and become a source of repeat business. Even purchasers who elect to rescind because of defects unflinchingly disclosed may look to the same broker for assistance in locating a more suitable home.

An Ohio study added further support to the notion that buyers' comfort levels with their acquisitions increase when they feel they have been told the truth about the property.⁸³ In 1993, Ohio enacted a seller disclosure law. The study questioned one group of Ohio home buyers in 1990, before the enactment of the law, and a comparable group of buyers in 1996, after enactment of the law. Roughly two-thirds of the buyers in both survey years reported having received a home of the construction quality they had expected. Disclosure made a statistically significant difference in buyers' post-sale satisfaction rates. The number of buyers disappointed with their acquisitions after the closing dropped from fifteen percent before the statute was enacted to five percent afterwards.⁸⁴

Brokers and scholars of law and economics agree that disclosure has the potential of increasing home prices.⁸⁵ Understandably, buyers seek price reductions to offset the costs of repairing disclosed defects. By the same token, buyers pay more for homes free of defects. Absent a reliable system of full disclosure, buyers do not know whether the home is defect-ridden or defect-free when making their offers. Rational buyers would be expected to discount offer prices to account for the possibility that they were bidding on a home with concealed faults. Once a trustworthy system of seller disclosure is put into place, buyers will offer more for homes reported to be in good condition.

Seller disclosure has not put an end to all "undisclosed defect" litigation. Indeed, the general counsel of one of southern California's largest brokerage firms reports that although he has seen a sizable reduction in the number of claims per transaction, ninety to ninety-five percent of all

⁸³ See Gary S. Moore & Gerald Smolen, *Real Estate Disclosure Forms and Information Transfer*, 28 REAL EST. L. J. 319, 326 (2000) ("[T]he average seller may obtain a better price because of the elimination of a portion of the uncertainty associated with the sale of an asset with unknown attributes.").

⁸⁴ See *id.* at 331-32.

⁸⁵ See Michael J. Fishman & Kathleen M. Hagerty, *Mandatory Versus Voluntary Disclosure in Markets with Informed and Uninformed Customers*, 19 J. L. ECON. & ORG. 45, 47 (2003) (finding informed consumers pay more for higher quality products). NAR has advanced the argument that full disclosure would result in sales prices more accurately reflecting true market value. See NAT'L ASS'N OF REALTORS, PROPERTY CONDITION DISCLOSURE, *supra* note 81, at 5.

claims currently filed against the firm are for alleged disclosure failures.⁸⁶

Buyers continue to file claims for many reasons. Some brokers and sellers simply neglect to make any of the requisite disclosures. Others deliberately hide matters that should have been disclosed⁸⁷ or engage in fraud.⁸⁸ They may advise buyers against obtaining independent home inspections⁸⁹ or urge sellers to obtain second opinions from pest control experts, home inspectors, or geologists when the first inspection report is unfavorable, then show prospective buyers only the second favorable report.⁹⁰ One litigator reports that every buyer he represents, including those who received perfectly adequate seller disclosure, adamantly insists the broker downplayed disclosed defects, convincing the buyer to disregard them.⁹¹ Some lawsuits are filed by buyers' seizing upon modest imperfections disclosed by the seller as a convenient excuse for backing out of a deal.⁹²

V. THE ORIGIN OF SELLER DISCLOSURE STATUTES AND THE BROKER'S INDEPENDENT DISCLOSURE OBLIGATIONS

California was the first state where brokers successfully lobbied for a statute mandating the use of property condition disclosure forms. The brokers lobbied the legislature in 1985 following a landmark case, *Easton v. Strassburger*,⁹³ which extended broker liability in two ways. *Easton* delivered a message to California real estate agents selling residential listings that: (1) Real estate agents would have an obligation to inspect the

⁸⁶ Telephone Interview with Mike Hull, General Counsel, Coldwell Banker, Southern California (July 2, 2003). Mr. Hull has held this position for fourteen years.

⁸⁷ See, e.g., *Miles v. McSwegin*, 388 N.E.2d 1367 (Ohio 1979) (finding a broker liable to a buyer for costs of termite extermination because he failed to disclose the lender's unfavorable termite report to the buyers before the closing).

⁸⁸ Telephone Interview with Mike Hull, *supra* note 86.

⁸⁹ See *Vuljak v. Pandele*, 2002 WL 991014 (Cal. App. 2002).

⁹⁰ See *Gilbert v. Corlett*, 339 P.2d 960, 960 (1959) (finding the seller was obligated to disclose an earlier report that the house would eventually become uninhabitable once he provided a later, favorable engineer's inspection report to buyer). See also *Radakovich v. Fila*, No. GD 93-12049 (C.P. Allegheny Pa. 1993). The brokers and sellers never disclosed an earlier radon test results to the buyers, which showed high levels of radon contamination. They presented to the buyers only the results of a test showing an acceptably low level of radon.).

⁹¹ Telephone Interview with Ron Rossi, Attorney and Real Estate Columnist, San Jose Mercury News (Aug. 7, 2003).

⁹² Mike Hull estimates that claims rise by ten to twenty percent when real estate prices are declining. Telephone Interview with Mike Hull, *supra* note 86.

⁹³ See 199 Cal. Rptr. 383 (Ct. App. 1984).

property for sale and relay the results of that inspection to prospective buyers, and (2) in addition to checking out the physical condition of the property, real estate agents would be required to disclose to buyers not only known or recently discovered information, but also any and all "facts materially affecting the value or desirability of the property . . . which through reasonable diligence should be known" to the agent.⁹⁴

In *Easton*, the Strassburgers purchased the property in 1972, and shortly afterwards, built a home and swimming pool and converted a barn into a guest house. In 1973 and 1975, the Strassburgers placed netting on a slope to repair damage caused by major landslides. The Strassburgers also constructed a retaining wall, which was not finished by the time they entered escrow with the buyer, Mrs. Easton. Instead of telling Mrs. Easton about the landslides they had experienced, the Strassburgers answered "no" on a broker-administered property information sheet that specifically asked if the sellers were aware of any past soil subsidence or settlement problems.⁹⁵

The uneven floor and hillside netting were plainly visible in the sales brochure photos. Had these clues of soil problems troubled Mrs. Easton enough to hire a geologist, she probably would have learned about the potential for recurrent landslides. But she did not hire a geologist. Mrs. Easton admitted knowing the lot was "cut and fill," but she had no idea that the soil was soft adobe and the fill was poorly compacted. Within two years of the closing, a landslide undermined the driveway and threatened the stability of both the house and guest house.⁹⁶

Prior to the sale, one of the agents admitted noticing an uneven floor in the guest house, a common indicator of soil problems (although an uneven floor could be caused by a bad framing job, lack of sufficient support beams, advanced termite infestation, earthquake, or water damage). One or both of the agents involved in the transaction knew that the house was built on fill and that erosion problems commonly occur on improperly compacted fill. Both agents kept this knowledge to themselves and never advised the buyer to hire a geologist to check soil stability.⁹⁷

Once the landslides occurred, Mrs. Easton sued everyone potentially liable in the transaction, including the sellers, the listing and selling

⁹⁴ Debra L. Fink, *A Legislative Response to Easton v. Strassburger*, 4 CAL. R. PROP. J. 18, 19 n.12 (1986) (citing language from the jury instruction approved on appeal by the *Easton* court).

⁹⁵ See *Easton*, 199 Cal. Rptr. at 385.

⁹⁶ See *id.*

⁹⁷ See *id.* at 386.

brokers, and both the developer and builder who had constructed the home. Mrs. Easton's purchase price was \$170,000, but in its damaged condition, the property could have been worth as little as \$20,000, with repair estimates ranging as high as \$213,000.⁹⁸

Under California's comparative negligence rules, the jury found the sellers sixty-five percent responsible, the builder twenty-five percent responsible, the listing broker five percent responsible, and the cooperating broker (not a party to the litigation) five percent responsible.⁹⁹ In comparative negligence situations, joint and several liability applies.¹⁰⁰ Because the sellers, the developer, and the builder were judgment-proof, the listing agent had to pay the entire judgment, which the listing agent later split with the selling broker.¹⁰¹ Clearly, the agent's loss far exceeded the agent's commission.

By March 1985, the California Association of Realtors had published a five point preventive program for real estate licensees to guide them in how to stay clear of *Easton*-type liability.¹⁰² According to the guidelines, real estate licensees should: (1) Ask sellers about property defects; (2) inspect the property; (3) disclose the results in writing to buyers; (4) discuss the inspection report with buyers; and (5) recommend further action based on the disclosure. The pamphlet came with a standard disclosure form. A statute imposing almost the same requirements became effective January 1, 1986.¹⁰³

The justifications for this broker liability standard are varied. First, buyers expect a certain standard of conduct from the listing broker as a licensed, competent professional. As NAR noted over a decade ago, the inspection, which typically takes one to two hours, "[I]s probably quite similar or essentially identical to that which conscientious agents ordinarily make to familiarize themselves with the property and its features."¹⁰⁴

⁹⁸ See *id.* at 385.

⁹⁹ See *id.* at 386.

¹⁰⁰ See *Am. Motorcycle Ass'n v. Super. Ct.*, 578 P.2d 899, 901 (Cal. 1978).

¹⁰¹ See *Easton*, 199 Cal. Rptr. at 396. After the case was concluded, the listing broker secured a settlement with the selling broker equal to approximately half the actual damages. E-mail from Victoria B. Naidorf, Vice President and Brokerage Counsel, Coldwell Banker, Northern California, to George Lefcoe (Aug. 29, 2003).

¹⁰² See generally Paula C. Murray, *The Real Estate Broker and the Buyer: Negligence and the Duty to Investigate*, 32 VILL. L. REV. 939 (1987).

¹⁰³ See CAL. CIV. CODE § 2079.5 (West 2004).

¹⁰⁴ NAT'L ASS'N OF REALTORS, PROPERTY CONDITION DISCLOSURE, *supra* note 81, at 7. See also Paula C. Murray, *supra* note 102, at 983.

A rule protecting a broker who had not bothered to take a close look at the property and requiring only disclosure of known defects, but not defects reasonably discoverable, would wrongly protect a broker from "his ignorance of that which he holds himself out to know."¹⁰⁵ If brokers do not have a duty to discover defects, brokers may have a perverse incentive to remain ignorant because "inspections might reveal information decreasing the home's value."¹⁰⁶ Requiring buyers to prove the broker's actual knowledge when they believe they have been deceived could inadvertently shield negligent brokers from their own incompetence or deceit.

Holding brokers to this higher standard may have the additional advantage of discouraging them from advising sellers to make a house more saleable by painting over or covering up evidence of serious defects without making the requisite disclosures because once brokers learn of defects, even after the removal of visible evidence, they would be required to share their knowledge with prospective buyers.

Mandated broker inspections and disclosures can also provide a discreet way for listing brokers to correct errors in the sellers' disclosure form without putting them in the compromising position of having to offer on their own initiative a correction of their sellers' errors or omissions.

Following *Easton*, some states imposed an inspection obligation on real estate agents or held them accountable for what they should have known.¹⁰⁷ The states that require independent broker inspections for the benefit of buyers include California, Maine,¹⁰⁸ New Jersey,¹⁰⁹ New Mexico,¹¹⁰ Wisconsin,¹¹¹ and, possibly, Utah.¹¹² Seven states have firmly

¹⁰⁵ *Easton*, 199 Cal. Rptr. at 388.

¹⁰⁶ Note, *Imposing Tort Liability on Real Estate Brokers Selling Defective Housing*, 99 HARV. L. REV. 1861, 1869 (1986) (citing Anthony Kronman, *Mistake, Disclosure, Information, and the Law of Contracts*, 7 J. LEGAL STUD. 13-14 (1978)).

¹⁰⁷ See cases collected in Annotation, *Real-Estate Broker's Liability to Purchaser for Misrepresentation or Nondisclosure of Physical Defects in Property Sold*, 46 A.L.R.4th 546 (1986).

¹⁰⁸ See Washburn, *supra* note 37, at 415-16. Chapter 330 of Maine's Real Estate Commission Rules require licensees to fill out a disclosure statement concerning the property's private water supply, insulation, waste disposal system and any known hazardous materials. See ME. DEP'T OF PROF. AND FIN. REG., REAL ESTATE COMM'N, 02-039 Ch. 330, §§ 16-19 (2002), at <http://www.state.me.us/sos/cec/rcn/apa/02/chaps02.htm> (last visited June 1, 2004). This may be taken to imply a broker inspection obligation.

¹⁰⁹ The New Jersey Supreme Court has held that listing brokers have a duty to conduct a reasonable inspection in connection with their open houses and to warn prospective buyers of reasonably discoverable latent defects of which the broker has actual knowledge. See *Hopkins v. Fox & Lazo Realtors*, 625 A.2d 1110, 1120-21 (N.J. 1993).

¹¹⁰ See *Gouveia*, 686 P.2d at 265 ("Under some circumstances, a broker may have a

limited broker disclosure obligations to matters demonstrably within the brokers' actual knowledge.¹¹³

NAR's Code of Ethics has for a long time contained language admonishing brokers not to exaggerate, misrepresent, or conceal.¹¹⁴ But in the year following the *Easton* decision, NAR amended its Code of Ethics to delete any mention of an "affirmative obligation to discover adverse factors that a reasonably competent and diligent investigation would disclose"¹¹⁵—the duty to inspect language quoted in *Easton*.¹¹⁶ NAR replaced the deleted inspection requirement with the statement that Realtors shall not be "obligated to discover latent defects in the property or to advise on matters outside the scope of their real estate license."¹¹⁷

duty to disclose defects that an inspection would reveal.").

¹¹¹ See WIS. STAT. ANN. § 452.23(2)(b) (West 1998) (relieving broker from the duty to inspect if there is a professional home inspection).

¹¹² See Secor v. Knight, 716 P.2d 790, 795 n.1 (Utah 1986) (citing with approval, in dicta, *Easton*'s requirement that brokers disclose to buyers material facts known or "through reasonable diligence should be known to him.").

¹¹³ See, e.g., IOWA CODE ANN. § 558A.6(1) (West 2002) ("The transferor, or a broker or salesperson, shall not be liable under this chapter for the error, inaccuracy, or omission in information required in a disclosure statement, unless that person has actual knowledge of the inaccuracy, or fails to exercise ordinary care in obtaining the information."). See also Herbert v. Saffell, 877 F.2d 267, 274 (4th Cir. 1989) (finding no *Easton* duty for a broker to inspect under Maryland law); Aranki, 979 P.2d at 536 ("The duty of fair dealing does not include investigations to discover defects in the sellers' property."). Similar holdings can be found in Alabama, Illinois, Oklahoma, Texas, and West Virginia.

¹¹⁴ See recent versions of NAT'L ASS'N OF REALTORS, CODE OF ETHICS AND STANDARDS OF PRACTICE art. 9 (1988-2000) [hereinafter CODE OF ETHICS] (on file with author).

¹¹⁵ *Id.* art. 9 (1986). Compare Johnson v. Geer Real Estate Co., 720 P.2d 660, 666 (Kan. 1986) (finding a broker liable to buyers for selling buyers a house on a septic tank when they said they were not interested in a house served by a septic tank because the broker had relied on sellers' representation that the house was served by city sewers) with Lyons v. Christ Episcopal Church, 389 N.E.2d 623, 625 (Ill. App. Ct. 1979) (holding free from negligent misrepresentation a broker free who had relayed the sellers' assurances to the buyer that the house was hooked up to city sewers when it was not; the buyers were allowed to recoup the costs of the hookup from the sellers, but the broker was exonerated because they found that brokers have no "duty . . . to independently substantiate the representation of a disclosed seller.").

¹¹⁶ See *Easton*, 199 Cal. Rptr. at 388.

¹¹⁷ CODE OF ETHICS, *supra* note 114, art. 9 (1987). Effective in 1993, the Code added "or to disclose facts which are confidential under the scope of agency duties owed to their clients." Subsequently adopted Codes in 1995 and 2000 have retained the 1993 version on this point except that in 1995, this provision was relocated from article 9 to article 2, and in 2000, article 2 was amended to add that brokers were not obligated to disclose confidential

A good case can be made for limiting broker liability as indicated in the modified NAR Code of Ethics and confining the broker's disclosure obligation to matters within the scope of the broker's training as a professional licensee. Courts hold brokers only to the standard of care of a real estate licensee.¹¹⁸

State licensing exams for real estate salespersons and brokers do not test brokers on construction techniques and methods.¹¹⁹ Most brokers have no formal training in the construction trade, surveying, or engineering.¹²⁰ Exposing them to liability for not appreciating the nuances of these disciplines would be unfair and futile.¹²¹ A good residential broker tracks sales prices in the market area and can extrapolate data from recent sales to make an educated guess about the price at which a home is likely to sell. Brokers may be familiar with the characteristics of the neighborhoods they cover, the home improvements most likely to increase sales prices enough to justify making them, and the features that enhance a home's curb appeal. But as real estate licensees, brokers are not expected to know much about construction of a home, except for a few basic construction terms and the popular designation of architectural styles (the ability, for instance, to spot a mid-century house). The typical real estate agent has "no formal education or career expertise at all in the construction trades (e.g., plumbing, electrical, masonry), in surveying, structural and other engineering fields, in financing, and/or in law."¹²² At most, brokers may recognize evidence of potential problems—water stains, rotted beams, cracked stucco, damp walls, or dirty pool water. Brokers' obligations to buyers end when they point these out, alerting the prospective buyers of the need to find an appropriate expert to analyze the damage and suggest cures for the troubling symptoms.

Should brokers receive more training in construction methods? "That would be a bad idea," cautions June Barlow, Vice President and General Counsel, California Association of Realtors, "[Because] a sales agent who

facts "under the scope of agency or non-agency relationships as defined by state law."

¹¹⁸ See, e.g., CAL. CIV. CODE § 2079.2 (West 2004) (defining the statutory standard of care as the degree of knowledge required to secure a real estate license).

¹¹⁹ See, e.g., CAL. DEP'T OF REAL EST., INSTRUCTIONS TO LICENSE APPLICANTS (Jan. 2002), available at http://www.dre.ca.gov/pdf_docs/re4.pdf.

¹²⁰ See Ann Morales Olazabal & Rene Sacasas, *Real Estate Agent as 'Superbroker': Defining and Bridging the Gap Between Residential Realtors' Abilities and Liabilities in the New Millennium*, 30 REAL EST. L. J. 173, 229 (2000).

¹²¹ See *id.* at 229.

¹²² *Id.*

purports to act as if she were a knowledgeable home inspector or contractor will be held to the standard of care of those professions.”¹²³

The defects a professional home inspector is capable of spotting are vastly different from those a broker is likely to notice. Few brokers, or sellers for that matter, would notice, for example:

[W]hen safety violations exist in electric panels, such as overfused circuits or a bonded neutral buss in a subpanel, if outlets are ungrounded, if the forced air furnace has a cracked heat exchanger, emitting carbon monoxide into the home, whether the drain pipes beneath their homes are leaking, not properly installed, corroded, damaged or have been improperly modified.¹²⁴

The list of defects a trained building inspector would catch, but that most sellers and brokers would miss, could go on for pages.

Most buyers understand that a seller’s account of property defects could be biased, even if a seller is making every attempt to tell all. A seller’s desire to sell could skew the seller’s perceptions of the property’s shortcomings. Besides, sellers need only disclose what they know. Not being experts in construction, they may not discern all the home’s defects. But when brokers are required to reveal their own observations about the condition of the property, some buyers may place too much confidence in the broker’s disclosure and be lulled into believing they can do without a professional inspection.¹²⁵ Seller disclosure forms eliminate this by explicitly alerting buyers of the need for professional home inspections.

Realtors have concluded that the best way of dealing with *Easton*-type exposure to liability is to shift the primary responsibility for property disclosures from brokers to sellers and to insist buyers hire professional home inspectors.¹²⁶ Most Realtor-drafted forms make it abundantly clear that the property condition disclosure is no substitute for the buyer’s due diligence. Forms insistently urge: “BUYER SHOULD OBTAIN PROFESSIONAL

¹²³ Interview with June Barlow, Vice President and General Counsel, California Association of Realtors, in Los Angeles, Cal. (July 30, 2003). *See also* 2 HARRY D. MILLER & MARVIN B. STARR, CALIFORNIA REAL ESTATE § 3:52 (3d ed. 2002) (stating that brokers who engage in the unauthorized practice of law are held to the same standard of care as an attorney).

¹²⁴ Barry Stone, *House Detective*, SAN DIEGO UNION-TRIB., Jan. 5, 2003 at I6.

¹²⁵ The chance of buyers’ making this mistake appears greatest among those with the lowest incomes. *See* Karen Eilers Lahey & David A. Redle, *The Ohio Experience: The Effectiveness of Mandatory Real Estate Disclosure Forms*, 25 REAL EST. L.J. 319, 329-30 tbl. 12 (1997).

¹²⁶ *See* Telephone Interview with Ralph W. Holmen, Associate General Counsel, National Association of Realtors (Aug. 4, 2003).

ADVICE AND INSPECTIONS OF THE PROPERTY TO MORE FULLY DETERMINE THE CONDITION OF THE PROPERTY.”¹²⁷ The Utah Association of Realtors goes well beyond this and presents buyers with a two page, single spaced property checklist containing sixteen numbered items, each pointing to an area of inquiry the buyer would be well advised to pursue, including building code or zoning compliance, surveying, geologic conditions, mold, water availability, property taxes, and income tax or legal consequences.¹²⁸

Fortunately, as the use of property condition disclosure forms has become commonplace, more buyers than ever are yielding to the repeated entreaties of Realtors and are hiring home inspectors to check the items signaled for attention in the disclosures presented to them. In the years following the enactment of California’s property condition disclosure law, the use of independent home inspectors tripled.¹²⁹ According to a recent study, seventy-seven percent of home buyers had inspections done before buying.¹³⁰

¹²⁷ STATE OF MICH. SELLER’S DISCLOSURE STATEMENT 2 (2000) (on file with author). The Coldwell Banker California Disclosure Obligation Forms caution buyers not to rely solely on what sellers or real estate agents tell them about the property. The forms warn that required written disclosures do not take the place of hiring expert inspectors to evaluate the size, condition, and use of the property, including but not limited to governmental requirements and limitations, geological and environmental hazards, structural and non-structural systems, waste disposal, water and other utility systems and components, neighborhood conditions, and personal preference factors. Securing disclosure information does not take the place of maintaining the property after escrow closes nor is there a guarantee that changes in those issues will not occur. Buyers have an obligation “to exercise reasonable care to protect [themselves], including those facts which are known to or within the diligent attention and observation of the buyer” under CAL. CIV. CODE § 2079.5 (West Supp. 2004). When any problem is noted in a disclosure or inspection report, buyers should retain appropriate experts to determine the extent of the problem and the proper means for and the cost of correcting that problem before escrow closes. Buyers are encouraged personally to verify the condition and uses of the property and the seller’s compliance with all contractual provisions prior to the close of escrow. See COLDWELL BANKER RESIDENTIAL BROKERAGE Forms (on file with author).

¹²⁸ See UTAH ASS’N OF REALTORS, PROPERTY CHECKLIST (2003) (on file with author).

¹²⁹ See Linda Lipman, *Inspector’s Eye*, SAN DIEGO UNION-TRIB., Dec. 19, 1993, at H1 (noting that inspections tripled from twenty to sixty percent following the enactment of CAL. CIV. CODE § 1102).

¹³⁰ See Donna Halvorsen, *Disclosure Law: New State Law Compels Disclosure; Starting Jan. 1, Sellers Must Reveal Problems, But Buyers Still Will Have Few Remedies*, STAR TRIB., June 1, 2002 (quoting Glen Dorfman, Minnesota Realtors Association’s Executive Officer), available at 2002 WL 5375981 (referring to a nationwide study conducted jointly by the National Association of Realtors and the American Society of Home Inspectors.).

VI. A COMPARISON OF SELLER DISCLOSURE FORMS

A. Who Should Promulgate the Forms: State Legislatures, State Regulatory Agencies or Local Realtors?

The property condition disclosure form may be embedded in a disclosure statute, drafted by the state agency responsible for broker licensing, or written by state and local Realtors associations or brokerage firms. Often, lawyers prefer using statutory forms, relying upon them as safe harbors, an assured way of achieving full compliance with the law. But in this situation, no safe harbors can be found because the disclosure statutes do not purport to pre-empt the evolving common law. Sellers remain obligated to disclose all known material latent defects—whether mentioned in the form or not.

Sellers can be woefully misled by the way the statutory form phrases the seller's disclosure obligation. Real estate attorney Victoria B. Naidorf¹³¹ points out that California's statutory form asks whether the seller is "aware of any significant defects/malfunctions."¹³² But many defects that the seller may personally regard as insignificant or previously repaired are nonetheless required to be disclosed. The common law in California, before and after the statute's enactment, calls for the seller to reveal all known facts materially affecting the value or desirability of the property. To ensure the seller understands what this means, brokers in several northern California counties supplement the statutory form with a questionnaire that cautions sellers to disclose "if [they] are aware of any condition or circumstance, whether past or present, and whether or not previously repaired," regarding several hundred items, ranging from cracks in foundation walls to defects in the hardwood floors (e.g., stains or warping).¹³³ Another local Realtors association uses a supplemental questionnaire asking sellers if they are aware of any "inspections conducted, or reports or repair estimates prepared" regarding sixteen listed items, ranging from pest control to natural hazards.¹³⁴

¹³¹ Telephone Interview with Victoria B. Naidorf. Her work includes advising the 4500 Northern California Coldwell Banker sales agents on property condition disclosures.

¹³² CAL. CIV. CODE § 1102.6 (West Supp. 2004).

¹³³ SAN FRANCISCO ASS'N OF REALTORS, PRDS SUPPLEMENTAL SELLER CHECKLIST 1 (2000) (on file with author). This list is used in Santa Clara, San Mateo, and parts of other neighboring counties. Letter from Victoria B. Naidorf, to George Lefcoe (Aug. 25, 2003).

¹³⁴ SAN FRANCISCO ASS'N OF REALTORS, SELLER'S SUPPLEMENT TO THE REAL ESTATE TRANSFER DISCLOSURE STATEMENT (2001) (on file with author). Letter from Victoria B. Naidorf, *supra* note 133.

When California's Property Condition Disclosure Law was enacted, California's Realtors lobbied for the disclosure form to be imbedded in the statute "to make amendments to the form more difficult to achieve."¹³⁵ While encouraging predictability, a significant shortcoming of this proposal was that legislatures seldom bother to update statutory forms each time they mandate new items to be disclosed. For instance, after promulgating its statutory form, California adopted legislation calling for disclosure of whether the property was zoned for or affected by an industrial use¹³⁶ and whether an occupant had died on the premises within three years of the purchase offer.¹³⁷ But the statutory disclosure form has not been redrafted to keep up with these new laws. So the form has become an unsafe harbor—except when updated regularly with special supplementary questionnaires, such as those that California Realtors have been promulgating.

Most lawyers who work with real estate agents believe the best forms are those promulgated by state real estate commissions or Realtors associations. Forms drafted by state agencies appear more authoritative, less subject to bias in favor of real estate brokers, and more likely to be taken as convincing evidence the broker met the requisite standard of care. But state administrators may be slower, more vulnerable to lobbying efforts by opponents of mandated seller disclosures,¹³⁸ and less flexible than Realtor associations in making needed revisions. For instance, the most recent version of the Arizona Association of Realtors form added a question about pesky animals and insects in response to numerous lawsuits alleging seller failures to disclose the presence of scorpions on the property.¹³⁹ Another example comes from Utah where, not long ago, brokers became aware of increasing buyer complaints about undisclosed mold problems.

¹³⁵ NAT'L ASS'N OF REALTORS PROPERTY CONDITION DISCLOSURE, *supra* note 81, at 39.

¹³⁶ See CAL. CIV. CODE § 1102.17 (West Supp. 2004).

¹³⁷ See CAL. CIV. CODE § 1710.2 (1998).

¹³⁸ See Carolyn L. Mueller, Legislative Notes, *Ohio Revised Code Section 5302.30: Real Property Transferor Disclosure—A Form Without Substance*, 19 U. DAYTON L. REV. 783, 822-23 (1994) (stating that the Ohio State Bar Association and the American Association of Retired Persons blocked adoption of a statutory form and, when the task of drafting a form was delegated to the state Commerce Department, were instrumental in persuading the Department to reduce the number of topics included).

¹³⁹ See Macario Juarez, Jr., *Taking Aim at Home Defects*, ARIZ. DAILY STAR, Feb. 26, 2002, at D1. ("Seen any scorpions, bee swarms, owls or rabid animals on your property? How about mold? If so, the Arizona Association of Realtors wants to know on a newly revised disclosure statement it asks of home sellers.").

Within forty-five days, the Utah Association of Realtors revised their property condition disclosure form to incorporate a series of questions regarding mold. Had the form been statutory, it would have taken a year and a half to change, according to David W. Johnson, counsel to the Utah Association of Realtors, and the process would have been "more painful than a root canal."¹⁴⁰

B. Should Seller Disclosure Be Mandated by Statute or Not?

Over two-thirds of states mandate seller disclosure by statute. Mandated seller disclosure statutes have some distinct advantages. Generally, sellers are more likely to provide written property disclosures that have been mandated by statute.¹⁴¹ Statutorily mandated disclosure also protects conscientious brokers from unfair competition by rivals trying to snare listings by convincing sellers they do not need to fill out the disclosure form.¹⁴²

The integrity of a disclosure system depends on high rates of seller compliance because when few sellers comply, buyers may not know what to make of the disclosures they do receive.¹⁴³ Consider the myriad possibilities. Should buyers assume that sellers, who are not willing to fill out a property condition disclosure form, have something to hide or just that non-complying sellers have been cautioned by their attorneys against increasing their exposure to later claims of misrepresentation for innocent omissions? Where disclosure compliance rates are low, buyers could assume there is a selection bias resulting in a higher frequency of disclosures from sellers of relatively trouble-free houses, and thus reduce their bids on homes being sold without an accompanying seller disclosure

¹⁴⁰ Telephone Interview with David W. Johnson, Counsel to the Utah Association of Realtors (Aug. 4, 2003).

¹⁴¹ For instance, before California collected six requirements into one statute and made listing agents the guarantors of compliance, approximately ten percent of transactions included a natural hazards disclosure. After these changes, compliance rates increased to ninety percent or more. Telephone Interview with Sergio Siderman, Vice President and General Counsel, Property I.D. Corporation (June 27, 2003). Property I.D. Corporation is the preeminent disclosure firm in California, and it prepares about one-half the natural hazard disclosure forms purchased by home sellers state-wide. *See also* Moore & Smolen, *supra* note 83, at 326 (explaining that the use of property condition disclosures was far more frequent after Ohio enacted a mandatory seller property condition disclosure statute).

¹⁴² Telephone Interview with Ralph W. Holmen, Associate General Counsel, National Association of Realtors (Aug. 4, 2003).

¹⁴³ See DOUGLAS G. BAIRD ET AL., GAME THEORY AND THE LAW 97-109 (1994).

form.¹⁴⁴ Buyers would be uncertain whether the homes of sellers voluntarily disclosing numerous defects are more or less defect-ridden than homes of non-disclosing sellers. Maybe disclosing sellers are just more honest. These uncertainties are minimized when buyers receive completed, standard property condition disclosure forms from all, or nearly all, sellers.

Substantial compliance rates can be secured by means other than the enactment of a property condition disclosure statute. Currently, fifteen states are without property condition disclosure statutes. Nonetheless, in most of these states, property condition disclosure forms, promulgated by Realtor associations or brokerage firms, are widely utilized. Sellers who dutifully sign Realtor-drafted purchase forms and listing agreements will find that these forms oblige them to fill out property condition disclosure forms.¹⁴⁵ In Utah, with limited exceptions, the legislature has empowered the state attorney general and the division of real estate to promulgate standard real estate forms.¹⁴⁶ Utah real estate licensees may use only these forms. Both the purchase and sale agreement and the listing agreement obligate the seller to provide a property condition disclosure. Utah compliance rates are high—estimated at upwards of seventy-five percent.¹⁴⁷ In Colorado, the real estate commission promulgated a property condition disclosure form, and virtually all sellers fill it out.¹⁴⁸ Use of the form has become so commonplace that most sellers probably assume they have no choice.

Besides mandating seller compliance, statutes can resolve countless

¹⁴⁴ See generally Katherine A. Pancak, Thomas J. Miceli, & C.F. Sirmans, *Residential Disclosure Laws: The Further Demise of Caveat Emptor*, 24 REAL EST. L. J. 291 (1996).

¹⁴⁵ Telephone Interview with Trey Goldman, Attorney, Governmental Affairs, Florida Association of Realtors (Aug. 9, 2003); Telephone Interview with Connie Denio, District Vice President and Chairperson of Forms Committee, New Mexico Association of Realtors (Aug. 7, 2003); Telephone Interview with Opal Evans, Risk Management Coordinator, Missouri Association of Realtors (Aug. 7, 2003); Telephone Interview with Ursula Krzywichka, Coordinator of Marketing and Communication, Massachusetts Association of Realtors (Aug. 7, 2003); Telephone Interview with Cici Osborne, Chairperson of Forms Committee, Georgia Association of Realtors (Aug. 7, 2003); Telephone Interview by Robert Cooper with Jeff Foster, Deputy Director of Colorado Real Estate Division (Aug. 4, 2003); Telephone Interview with Bill Yanek, Director of Governmental Affairs, Kansas Association of Realtors (July 29, 2003); Telephone Interview by Robert Cooper with Michael Moody, Director of Governmental Affairs, Alabama Association of Realtors (July 26, 2003); E-mail from Robert Golden, Association Executive, Vermont Association of Realtors, to Robert Cooper (July 26, 2003, 02:36:12 PST).

¹⁴⁶ See UTAH CODE ANN. § 61-2-20 (2000).

¹⁴⁷ Telephone Interview with David W. Johnson, *supra* note 140.

¹⁴⁸ Telephone Interview by Robert Cooper with Jeff Foster, *supra* note 145.

issues that could give rise to costly disputes. For instance, all statutes authorize some exemptions, most commonly for transfers by government entities, estate administrators, foreclosing lenders, court orders, transfers of new homes never occupied, or transfers between co-owners and spouses.¹⁴⁹ Some statutes specify a procedure for sellers to amend forms in order to correct errors or reveal newly discovered defects.¹⁵⁰ Some outline the precise procedure for completion and transmission of the form, including the role, if any, of brokers in the process.¹⁵¹ Under most statutes, after receiving the disclosure form, buyers are given a set period of time to rescind, usually limited to three days from receipt of the report.¹⁵² During this statutory disclosure rescission period, the deal is in limbo, but the rescission period will not cause any additional delay if the buyer receives the disclosure document well within the other contingency review periods provided in the contract for the buyer's home inspection, title review, and financing.

The statutes also prescribe remedies for non-compliance. The buyer's remedies depends on when the buyer discovers and protests undisclosed defects. Before closing, most statutes confer upon the buyer a right of

¹⁴⁹ See, e.g., IND. CODE ANN. § 32-21-5-1 (Michie 2002). In a few states, including Kentucky and Mississippi, the seller's property condition disclosure obligation only applies to transactions in which brokers are involved. Without broker assistance, many sellers would be unaware of their statutory disclosure obligation. However, this exemption tempts sellers with something to hide to avoid disclosure by marketing their homes themselves. See KY. REV. STAT. ANN. § 324.360(1) (Michie 2001) ("This section shall apply to sales and purchases involving single-family residential real estate dwellings if any person licensed under this chapter receives compensation"); MISS. CODE ANN. § 89-1-501(1) (1999) ("[P]rovisions . . . apply only . . . when the execution of such transfers is by, or with the aid of, a duly licensed real estate broker or salesperson.").

¹⁵⁰ See, e.g., CAL. CIV. CODE § 1102.5 (West 1998).

¹⁵¹ Compare IDAHO CODE § 55-2509 (Michie 2003) (stating that transferor delivers form to transferee) with N.J. STAT. ANN. § 56:8-19.1 (b)(3) (West 1985) (stating that the broker is not liable for relaying seller misrepresentations if broker makes visual inspection with reasonable diligence, obtains a report from seller, and informs the buyer that the seller is the source of all the information contained within it).

¹⁵² See ALASKA STAT. § 34.70.020 (Michie 2002) (allowing rescission three days after receipt or six days after statement is mailed); CAL. CIV. CODE § 1102.3(b) (West 1998) (allowing three days after receipt or five days after statement is mailed); HAW. REV. STAT. ANN. § 508D-5(b) (Michie 2000) (allowing fifteen days from receipt).

rescission.¹⁵³ Non-complying sellers cannot obtain specific performance.¹⁵⁴

If the buyer goes to closing without ever receiving a complete and truthful seller disclosure form, the buyer risks waiving a statutory right to rescind, but not a claim to actual damages for undisclosed defects or a common-law right to full disclosure.¹⁵⁵ Understandably, no property condition disclosure statute confers upon buyers a right of post-sale rescission.¹⁵⁶ A buyer's rescinding after closing would substantially burden the seller, because normally the seller will have relocated, paid off the existing mortgage loan, and possibly purchased a new home. Of course, for situations in which nothing but a post-sale rescission would make the buyer whole, the disclosure statute does not bar courts from granting such rescission.¹⁵⁷

To the relief of sellers and brokers, a handful of the statutes shorten the period within which claims can be filed for seller non-compliance to typically two years from the date of closing,¹⁵⁸ rather than the two to six

¹⁵³ However, if the contract's inspection contingency period exceeds the three day rescission under the disclosure statute, the buyer may have the longer period within which to rescind because of problems disclosed in the property condition statement. *See, e.g.*, *Minkovsky v. Felger*, No. B152806, 2002 WL 442265 (Cal. App. Mar. 21, 2002).

¹⁵⁴ *See generally* *Realmuto v. Gagnard*, 1 Cal. Rptr. 3d 569 (Ct. App. 2003) (stating the seller was denied the right to specific performance for not providing a transfer disclosure statement, thus depriving the buyer of the right to rescind within the statutory period).

¹⁵⁵ *See ALASKA STAT.* § 34.70.040 (Michie 2002); *IOWA CODE ANN.* § 558A.6 (West 2002); *MISS. CODE ANN.* § 89-1-523 (1972); *S.D. CODIFIED LAWS* § 43-4-42 (Michie 1997). A few states limit buyers to a fixed dollar sum when the seller provides no disclosure form (*e.g.*, *CONN. GEN. STAT. ANN.* § 20-327c (West 2002)).

¹⁵⁶ *See Hutchinson v. McCarty*, No. D039946, 2003 WL 21083850, at *6 (Cal. App. May 14, 2003). The seller never provided the required property condition disclosure form. The buyer had no right to rescind, but only the right to prove actual damages. The failure to comply with a disclosure statute did not invalidate the transfer.

¹⁵⁷ *See HAW. REV. STAT. ANN.* § 508D-16.5 (Michie 2000) ("Notwithstanding anything to the contrary in this chapter, any action for rescission brought under this chapter shall commence prior to the recorded sale of the real property."); *OKLA. STAT. ANN.* tit. 60, § 837B (West 1994) ("The sole and exclusive civil remedy at common law or otherwise for a failure under subsection A of this section by the seller or the real estate licensee shall be an action for actual damages. . . .").

In California, buyers have obtained post-sale rescission despite the statute's actual damage limitation when a court deemed rescission to be the only way to achieve equity for the buyer. *See Shapiro v. Sutherland*, 76 Cal. Rptr. 2d 101, 112 (Ct. App. 1998) ("Trial courts have broad equitable power to fashion any appropriate remedies."). *See also CAL. CIV. CODE* § 1102.13 (West 1998).

¹⁵⁸ *See CAL. CIV. CODE* § 2079.4 (West 1998) (stating two years from date of

years usually given to fraud or negligent claimants, which is measured from the date of discovery.¹⁵⁹ The shorter statutory period only applies to claims arising out of non-compliance with the disclosure statute. Thus, buyers retain the benefit of the longer statutes of limitations on claims predicated on fraud, misrepresentation, or breach of fiduciary duty.¹⁶⁰

C. What Questions Should Disclosure Forms Ask Sellers to Answer?

Seller disclosure forms usually are four to eight pages, single spaced. The forms vary considerably in the items covered. Most of the forms contain a list of appliances, fixtures, and some items of personal property (e.g., satellite dish, storage shed, microwave, window screens), which offers the seller a chance to disclose defects concerning these items. Some of the forms ask the seller to indicate whether the sale includes each item on the list,¹⁶¹ while others specify that the parties are to look just to the purchase and sale agreement for this information.¹⁶² A few are ambiguous as to whether the seller's checking a particular box means that an item is defective or indicates that it goes to the buyer along with the realty at closing.¹⁶³

recordation, date of close of escrow, or date of occupancy, whichever occurs first); HAW. REV. STAT. ANN. § 508D-17(a) (Michie 2000) (stating two years from receipt of disclosure statement or if none is received, two years from recorded sale.).

¹⁵⁹ See CAL. CIV. PROC. CODE § 338(d) (West 1979) (stating three years for fraud, measured from date of discovery).

¹⁶⁰ See *Field v. Century 21 Klowden-Forness Realty*, 73 Cal. Rptr. 2d 784, 786 (Ct. App. 1998). More than two years after acquiring the property, the buyer sued his broker for not properly disclosing a flood easement and for other breaches of fiduciary duty. The court declined to apply the two-year statute of limitations of the broker disclosure statute, which is measured from closing date, but instead utilized the "date of discovery" rule applicable to statute of limitations regarding suits against fiduciaries. See also *Williams v. Wells & Bennett Realtors*, 61 Cal. Rptr. 2d 34 (Ct. App. 1997). The buyer sued the broker for failure to disclose defects that the seller revealed to broker and covered up. The court held the applicable statute of limitations was for broker fraud, not for the broker's failure to comply with the property condition disclosure statute.

¹⁶¹ See ALA. REAL ESTATE COMM'N, RESIDENTIAL REAL PROPERTY TRANSFER DISCLOSURE STATEMENT 2 (2002) (on file with author); KAN. ASS'N OF REALTORS, SELLER'S PROPERTY DISCLOSURE STATEMENT 1 (1998) (on file with author); NEB. REAL ESTATE COMM'N, SELLER PROPERTY CONDITION DISCLOSURE STATEMENT 1 (2003) (on file with author); S.D. REAL ESTATE COMM'N, PROPERTY CONDITION DISCLOSURE STATEMENT 4 (on file with author).

¹⁶² See DEL. REAL ESTATE COMM'N, SELLER'S DISCLOSURE OF REAL PROPERTY CONDITION REPORT 1 (2000) (on file with author); MICH. ASS'N OF REALTORS, SELLER'S DISCLOSURE STATEMENT 1 (2000) (on file with author).

¹⁶³ See MISS. REAL ESTATE COMM'N, PROPERTY CONDITION DISCLOSURE STATEMENT

Most of the forms also list structural components, such as driveways, retaining walls, bearing walls, chimneys, windows, doors, exterior stucco, floors, foundations, roofs, sewer hook-ups, water systems, sump pumps, cut and fill, termite and rodent infestation. The better ones ask about the type of roof (e.g., asphalt, shingle, metal), its age, the date of the last repair or replacement, and whether the seller has had any specific problems with it, such as water leakage, ice damming, or other damage, and whether the seller has made any insurance claims based on such damage. A few forms ask the seller to name the contractors or inspectors who have worked on the site and provide their addresses and phone numbers, enabling buyers and their home inspectors to learn the history of the item from an informed source independent of the seller.¹⁶⁴

Typically, forms inquire about heating and air conditioning, plumbing and electrical systems. One state requires the following disclaimers: "What is the type of sewage system? . . . When was the on-site sewage disposal last serviced? . . . Is there a sewage pump?" Are the plumbing pipes copper, galvanized, lead, or PVC?¹⁶⁵

Title questions appear on a minority of forms, such as how long the seller has occupied the house, whether the seller knows of existing law-suits concerning the property, boundary or lot line disputes, whether the property is leased, whether there is a homeowners' association, any easements other than utility easements, any encroachments upon neighbor-

1 (2002) (on file with author).

¹⁶⁴ See KAN. ASS'N OF REALTORS, SELLER'S PROPERTY DISCLOSURE STATEMENT 2 (1998) (on file with author); MASS. ASS'N OF REALTORS, SELLER'S STATEMENT OF PROPERTY CONDITION 1 (1999) (on file with author); S.D. REAL ESTATE COMM'N, *supra* note 161, at 2; VT. ASS'N OF REALTORS, SELLER'S PROPERTY INFORMATION REPORT, 2 (2001) (on file with author).

Sometimes an inspection will reference prior work the seller claims to have done and will be made contingent on the seller's providing details concerning that work. In *Gordon A. Gundaker Real Estate Co. v. Maue*, the termite inspection noted that the owner had claimed the property was pretreated for termites, and the inspector "recommend[ed] [that the buyers] obtain 'details of the treatment, such as: the treatment date, company, any warranty information, copies of the contract and warranty, etc.'" 793 S.W.2d 550, 552 (Mo. Ct. App. 1990) (quoting the Stopke Pest Control termite report). The seller refused to provide this information, and the buyers terminated the contract. Because the termite inspection showed no signs of termites, the seller contended the buyers had no right to invoke the termite inspection contingency. At trial, testimony indicated "a high probability of [termite] infestation was legally equivalent to a report indicating actual termite infestation." *Id.* at 553.

¹⁶⁵ PA. ASS'N OF REALTORS, PENNSYLVANIA SELLER'S PROPERTY DISCLOSURE STATEMENT 2 (1997) (on file with author).

ing properties or of neighboring structures upon the subject property, or any planned road widenings.¹⁶⁶ A minority of forms also ask the seller to indicate the zoning classification, zoning violations, non-conforming uses, variances or conditional use permits, violations of setback requirements, and additions or conversions possibly made without building permits.

Some forms inquire about natural hazards, such as whether the property is within a Federal Emergency Management Agency ("FEMA") designated flood plain, or is located on or near an earthquake fault zone, a seismic safety zone, a wetland, a coastal barrier zone,¹⁶⁷ or an area of high fire-risk, or contains radon,¹⁶⁸ asbestos, lead-based paint,¹⁶⁹ or mold-contamination.¹⁷⁰

D. Should Property Condition Disclosure Forms Be Exhaustive or Abbreviated?

One might assume the shorter the form, the better off the seller is because shorter forms are quicker and easier to fill out. If fewer questions

¹⁶⁶ See, e.g., MASS. ASS'N OF REALTORS, SELLERS STATEMENT OF PROPERTY CONDITION 1 (1999) (on file with author).

¹⁶⁷ See David P. Hendricks, *Silence is Golden: The Case for Mandatory Disclosure of Coastal Hazards and Land-Use Restrictions by Residential Sellers in North Carolina*, 25 N.C. CENT. L. J. 96 (2002).

¹⁶⁸ Radon "is a colorless, odorless gas that seeps into buildings from the soil. . . . As a decay product of radium, radon is a granddaughter of uranium, which occurs widely in bedrock and soil. . . ." and the second leading cause of lung cancer—after smoking. MARK MONMONIER, CARTOGRAPHIES OF DANGER 174, 174-75 (1997).

The Environmental Protection Agency ("EPA") surveyed seventeen states in which twenty-five percent of all homes had elevated radon levels. "Today, radon problems and radon-contaminated homes have been identified in almost every state." Paul A. Locke & Patricia I. Elliott, *Caveat Broker: What Can Real Estate Licensees Do About Their Potentially Expanding Liability for Failure to Disclose Radon Risks in Home Purchase and Sale Transactions?*, 25 COLUM. J. ENVTL. L. 71, 73 (2000). Radon testing is inexpensive, homes can easily be designed and built to minimize radon risk, or existing homes retrofitted for \$2500 or less. "Because EPA's radon potential map is readily available, agents having access to such information would be pressed to argue that no duty of inspection arises." *Id.* at 84.

¹⁶⁹ Federal law bans enforcement of purchase and sale contracts for homes built before 1978, unless the seller provides the buyer a copy of a lead hazard information pamphlet prepared by the EPA, and discloses any known presence of lead-based paint. See Residential Lead-Based Paint Hazard Reduction Act of 1992, 42 U.S.C. § 4852d (2000).

¹⁷⁰ See HOUSTON ASS'N OF REALTORS, SELLER'S DISCLOSURE NOTICE (2002) (asking if seller is aware of "[a]ny repairs or treatment, other than routine maintenance, made to the Property to eliminate environmental hazards such as asbestos, radon, lead-based paint, urea-formaldehyde, or mold?") (on file with author).

are asked, there are fewer answers the seller will be tempted to lie about. But the more specifically referenced an item is in the questionnaire, the less likely is the forthright seller to overlook it. Remember, the seller's underlying common-law obligation, which survives these statutes, is to disclose all known material latent defects. Placing an item on the form creates a *prima facie* presumption of its materiality and, simultaneously, weakens any seller defense based on the patent-latent distinction. By filling out the form, the seller provides written evidence of representations, curtailing the "he said, she said" disputes that are typical in misrepresentation claims based on parol evidence. On the other hand, buyers cannot legitimately claim to have been surprised by defects clearly disclosed in a written form.

While the information can be useful to the buyer and the buyer's professional home inspector, information overload is an increasing concern.¹⁷¹ Each additional item or document required for sale competes with many others for the buyer's attention. For instance, in southern California, the seller disclosure form is just one of twenty-five separate disclosures the broker proffers,¹⁷² and this does not include the disclosures required of regulated lenders, the preliminary title report, and the pest control and home inspection reports.

E. Should Waivers and Disclaimers Be Permissible?

Some disclosure statutes allow sellers to opt out unilaterally,¹⁷³ some

¹⁷¹ See Coles, *supra* note 5, at 149 ("[I]nundating [buyers] with complex disclosures early on and a buffet of varying levels of representation adds only confusion instead of clarity.").

¹⁷² See CAL. ASS'N OF REALTORS, REAL ESTATE SALES DISCLOSURE CHART (2003) (on file with author).

¹⁷³ See MD. CODE ANN. REAL PROP. § 10-702(b)(1)-(2) (2003) (stating that a vendor has the option of giving buyer a disclaimer or a disclosure statement); OHIO REV. CODE ANN. § 5302.30(K)(3)(b), K(4) (Anderson Supp. 2002) (stating that if seller fails to provide form within thirty days, buyer may rescind or waives all rights under the disclosure statute); VA. CODE ANN. § 55-519A(1) (Michie 2003) (stating that seller can provide, in lieu of disclosure statement, "A residential property disclaimer statement . . . stating that the owner makes no representations or warranties as to the condition of the real property or any improvements thereon, and that the purchaser will be receiving the real property 'as is,' that is, with all defects which may exist, if any, except as otherwise provided in the real estate purchase contract"). A New York court has interpreted that state's disclosure law as allowing sellers to opt out completely by crediting the buyer with \$500 at closing, although the statute could be read as exposing the seller to actual damages for willful failure to comply. *See Malach v. Chuang*, 754 N.Y.S.2d 835, 841-42 (N.Y. City Civ. Ct. 2002). The Rhode Island Supreme Court has interpreted that state's disclosure law as prescribing a

require the buyers' consent,¹⁷⁴ and some prohibit waivers and disclaimers entirely.¹⁷⁵ Unfortunately, few statutes actually specify whether a pre-closing waiver is possible and, if so, whether the waiver must take any particular form.¹⁷⁶

Scholars are divided on whether sellers should be able to waive their common-law right to seller disclosure. Some scholars contend that sellers should be able to waive this right. They see no good reason to deny enforcement of a contract between a risk-averse seller and a risk-seeking buyer—the very model of an economically efficient transaction. When the parties have clearly specified that the buyer is to acquire the property without reliance on a seller disclosure statement, denying enforcement of their agreement injects an unwarranted element of legal uncertainty into the contracting process and may increase the chance of litigation. Unless sellers can protect themselves by contract against buyers who claim inadequate disclosure, sellers must adjust their prices upward or hold their properties off the market indefinitely. One scholar asserts that “[t]his would cut against the strong policy that encourages free alienability and discourages restraints on alienation which would have the effect of with-

\$100 administrative fine as the sole buyers' remedy against sellers who do not present disclosure statements. *See Stebbins v. Wells*, 818 A.2d 711, 716 (R.I. 2003).

¹⁷⁴ See ALASKA STAT. § 34.70.110 (Michie 2002) ("This chapter does not apply to the transfer of an interest in residential real property if the transferor and transferee agree in writing that the transfer will not be covered under this chapter."); MINN. STAT. ANN. § 513.60 (West Supp. 2004) ("The written disclosure required . . . may be waived if the seller and the prospective buyer agree in writing."); N.C. GEN. STAT. § 47E-2(11) (1985) (exempting transfer "when both parties agree not to complete a residential property disclosure statement"); TENN. CODE ANN. § 66-5-202(2) (Supp. 2003) (asserting that buyer must agree to waive the statutory disclosure).

¹⁷⁵ Act of June 12, 2003, ch. 328, §§ 1-6, 2003 Or. Laws 515 (removing the statutory disclaimer option).

¹⁷⁶ In California, the courts and legislature have barred the use of an "as is" clause as a disclaimer. *See CAL. CIV. CODE* § 1102.1 (West Supp. 2004) (stating explicitly the Legislature's intent to supersede *Loughrin v. Superior Court*, 19 Cal. Rptr. 2d 161, by providing that "the delivery of a real estate transfer disclosure statement may not be waived in an 'as is' sale"). The *Loughrin* case held the disclosure statute contemplated the possibility of a knowing waiver, but an "as is" clause would not suffice as evidence of the buyer's intent to waive statutory rights. Similar concerns should bar the use of an "as is" clause to eliminate broker liability. *See* Craig W. Dallon, *Theories of Real Estate Broker Liability and the Effect of the "As Is" Clause*, 54 FLA. L. REV. 395, 398 (2002) ("[C]ourts should not enforce exculpatory clauses in residential real estate sales contracts unless the broker can prove that the disclaimers were actually agreed to by the purchasers and that the clauses adequately identify the qualities disclaimed.") (emphasis omitted).

drawing property from the normal course and rules of commerce.”¹⁷⁷

A good case can be made against allowing waivers and disclaimers of seller disclosures. Rational risk allocation starts with a rational risk assessment. Even the best home inspector is likely to overlook some defects unless the seller reveals them or points the inspector in the right direction. No buyer can sensibly waive the seller’s disclosure until the buyer learns what the seller is trying not to disclose. Prohibiting buyers and sellers from negating the seller’s disclosure obligation does not stop the parties from agreeing to an enforceable “as is” clause disclaiming any seller representations or warranties—once the seller makes full disclosure. Without a seller disclosure followed by a thorough home inspection, buyers would not know what they were buying “as is.”¹⁷⁸

The circumstances under which a person could legitimately waive the right to truthful disclosure are difficult to imagine.¹⁷⁹ According to one commentator,

When a seller knows that disclosure of material information would correct a mistake as to a basic assumption by the buyer, and

¹⁷⁷ Roberts, *supra* note 12, at 45.

¹⁷⁸ Buyers who sign “as is” contracts are not excusing sellers from making full disclosure of known defects. No “economic assumption of risk” exists in real estate transactions, but “as is” buyers may be undermining their claim of reasonable reliance on the seller’s misstatements. Ann J. Rosenthal & R. Stuart Phillips, *Tell It Like It Is—Sellers’ Duties of Disclosure in Real Estate Transactions Under California Law*, 26 GOLDEN GATE U. L. REV. 473, 478 (1996). In *Alires v. McGhehee*, 85 P.3d 1191, 1200 (Kan. 2004), the buyers were denied damages against sellers who knew their basement leaked but lied about it in their disclosure form. The Kansas Supreme Court ruled that the buyers had no right to rely on the seller’s fraudulent disclosure statement because:

[T]he truth or falsity of the representation would have been revealed by an inspection of the subject property and the misrepresentations were made prior to or as part of the contract in which the buyer contracted for the right to inspect, agreed that the statements of the seller were not warranties and should not replace the right of inspection, declined inspection, and waived any claims arising from defects which would have been revealed by an inspection.

¹⁷⁹ Professor Florrie Roberts acknowledges this and provides a spirited case for allowing sellers to exculpate themselves from negligent misrepresentations. See Roberts, *supra* note 12, at 48-53. The trouble is that the distinction between fraudulent and negligent misrepresentation is often unclear. Allowing exculpation of negligent misrepresentation only increases the buyer’s litigation burden. It does not preclude the buyer from claiming fraud. Professor Roberts suggests that sellers should consider including an integration clause in the contract specifying exactly what representations were made, positioning the seller to argue for summary judgment if the buyer’s claim turns on representations other than those listed. See *id.* at 24-32.

when nondisclosure constitutes a failure to act in good faith and in accordance with reasonable standards of fair dealing, the withholding of information may be equated with, and given the same legal effect as, fraudulent misrepresentation.¹⁸⁰

Oregon recently repealed a disclaimer provision in its disclosure law for a number of interesting reasons. Like all the other disclosure statutes, Oregon's statute did not remove the seller's common-law obligation to disclose known material latent defects. Yet, many sellers were misconstruing the disclaimer election as if it had.

Realtors in Oregon were also troubled because sellers often received conflicting advice from their real estate agents and attorneys about whether to disclaim or disclose. Attorneys tended to recommend disclaimers to narrow the seller's exposure to legal risk. Real estate agents tended to encourage disclosure as a marketing tool to instill buyer confidence in the property. Realtors also observed the strong negative reactions of some buyers who took a disclaimer as a signal of a seriously defective property or an entirely untrustworthy seller.¹⁸¹ So, Oregon Realtors persuaded the legislature to eliminate the disclaimer option.

The language of disclosure forms must take into account whether sellers have the choice of opting out. In North Carolina, for instance, the disclosure statute extends to sellers the right to make "no representations as to the characteristics and condition of the real property or any improvements . . . except as otherwise provided in the real estate contract."¹⁸² Tracking this provision, the form prepared by the North Carolina real estate commission allows sellers to answer each question "Yes," "No," or "No Representation."¹⁸³

A few forms have been modified because earlier versions made the mistake of giving sellers what appeared to be a back door disclaimer by allowing them to answer "Yes," "No," or "Unknown." "Unknown" was deleted because some brokers were telling sellers they could not go wrong checking "unknown" as an answer to every question. This was bad advice because denial of knowledge the seller actually possesses is a misrepresentation. Unknown is not synonymous with no representation.

¹⁸⁰ Weinberger, *supra* note 51, at 400.

¹⁸¹ Telephone Interview by Robert Cooper with Matt Farmer, Associate General Counsel, Oregon Association of Realtors (July 17, 2003).

¹⁸² N.C. GEN. STAT. § 47E-4(a)(2) (2003).

¹⁸³ STATE OF N.C., REC. NO. 4.22, RESIDENTIAL PROPERTY DISCLOSURE STATEMENT 2 (2002) (on file with author).

F. Should a Seller-Provided Inspection Be an Acceptable Substitute for the Seller Disclosure Form?

A few disclosure statutes, such as Minnesota's, purport to relieve sellers of completing the property condition form if they substitute a professional home inspection in its place.¹⁸⁴ Two questions can be raised about statutory disclosure and home inspections: (1) Should sellers be relieved of their disclosure obligations if they pay for a professional home inspection? (2) Should the states impose an obligation on sellers to pay for a professional home inspection?

In response to the first question, the use of a professional home inspection does not replace the need for the seller's property condition disclosures. Without the seller's disclosures, many significant matters—from roof leaks to flawed foundations—could easily escape the attention of even the most astute inspector. According to one report, "Most inspections are based on visual observations only."¹⁸⁵ Inspectors are not required to enter dangerous areas of the property, inspect for rodents or hazardous substances, disassemble components, or drill holes in the wall or foundation. An inspector would not be able to test the air conditioner on a chilly winter day, pull up the carpets, remove wall hangings, or drag heavy furniture out of the way to look for hidden dry rot, water stains, or other evidence of defects.¹⁸⁶

Turning to the second question, Professor Robert Washburn endorses the idea of forcing sellers to pay for the home inspection. Professor Washburn states that "[i]f the cost is placed on the buyer, there is a problem with multiple inspections by successive buyers, each having to pay for the cost of an inspection."¹⁸⁷ Furthermore, the seller could obtain the report and make it available to the buyer before the listing broker begins showing the property to prospective buyers, enabling the buyer to adjust the purchase offers according to the revelations in the report instead of forcing

¹⁸⁴ Minnesota's statute, for instance, gives the seller an option of not filling out the disclosure form by providing "a written report that discloses the information" prepared by a government agency or any person the buyer or seller "reasonably believes has the expertise necessary to meet the industry standards of practice for the type of inspection or investigation that has been conducted by the third party in order to prepare the written report." MINN. STAT. ANN. § 513.56 3(a) (West 2004).

¹⁸⁵ Seth G. Weissman & Daliah Brill, *Call in a Professional Home Inspector for Pre-buy Visit*, ATLANTA BUS. CHRON., Feb. 7, 1997, available at <http://www.bizjournals.com/atlanta/stories/1997/02/10/focus24.html>.

¹⁸⁶ See Halvorsen, *supra* note 130.

¹⁸⁷ Washburn, *supra* note 37, at 444.

the buyer to re-trade the deal later, as the buyer often does following the buyer's own professional inspections. California real estate attorney John O'Reilly observes that many San Francisco real estate brokers urge sellers to pay for home inspections. Besides providing buyers with useful information, seller-funded inspections preempt buyers from renegotiating the price once in contract and encourage competitive bidding by increasing buyers' comfort levels.¹⁸⁸

Although the buyer is not made a party to the seller's agreement with the home inspector, the buyer will probably be able to enforce the seller's contract.¹⁸⁹ Even so, relying on the seller's inspection has drawbacks for the buyer. For starters, the buyer will seldom have been present during the inspection. The buyer's presence encourages a more thorough investigation and enables the buyer to ask the inspector's questions on the spot and the comprehend the inspector's observations and conclusions better. The buyer will not have participated in reviewing the terms of the inspection agreement, including provisions limiting the inspector's liability¹⁹⁰ and the buyer's time for filing a claim. Buyers will not know what the seller paid for the inspection, how long it took, and how careful the inspector was. Nor will the buyer have participated in selecting the inspector. The seller probably will shop around for an inspector with a reputation for not being too difficult—even though a lenient inspection does not absolve the seller from the legal obligation of disclosing all known material latent defects. Should the inspector present an alarming assessment of the property

¹⁸⁸ Email from John O'Reilly, Attorney, to George Lefcoe, Professor of Law, University of Southern California Law School (May 5, 2004).

¹⁸⁹ See *Hardy v. Carmichael*, 24 Cal. Rptr. 475, 480-81 (Ct. App. 1962) (holding the buyer entitled to damages against seller's negligent termite inspector).

¹⁹⁰ Many inspection firms contract to limit their liability to the fee paid for the inspection. Courts are divided on whether such clauses should be enforced. Compare *Schaffer v. Prop. Evaluations, Inc.*, 854 S.W.2d 493, 495 (Mo. Ct. App. 1993) (holding the limitation unenforceable; no evidence proved that any of the terms were specifically negotiated or that consideration was paid for the limitation of liability), and *O'Donoghue v. Smythe, Cramer Co.*, No. 80453, 2002 WL 1454074 at *5 (Ohio App. July 3, 2002) (finding the \$265 limitation of liability in conjunction with the arbitration clause stricken as unconscionable especially when contract called for arbitration and cost of arbitration would be at least \$500), with *Baker v. Roy H. Haas Assoc.*, 629 A.2d 1317, 1321 (Md. App. 1993) (holding a limitation enforceable in negligence action, but the limitation would not be enforced to protect the inspection firm against its own gross negligence), and *Peluso v. Tauscher Cronacher Prof. Eng'r's P.C.*, 704 N.Y.S.2d 289, 290 (App. Div. 2000) (upholding a \$445 limit of liability in the absence of special relationship between the parties, statutory provision, or overriding public interest, but finding the exculpatory limit would be inapplicable in the case of gross negligence).

condition, the seller will be tempted to seek a second opinion. The buyer may not know if the seller had discarded a previous, less favorable inspection report or instructed the inspector to exclude certain matters from the scope of the inspection.¹⁹¹ Buyers are well advised to be present when the inspection takes place.

For all these reasons, buyers overwhelmingly prefer to hire their own inspectors. Professor Weinberger doubts any savings can be achieved by seller inspections, and asserts that “[w]hile the occasional buyer may be willing to accept a seller’s disclosure and professional inspection report, most buyers will repeat the process by hiring their own inspectors, who will typically discover additional defects. This duplication of effort maximizes the parties’ joint transaction costs. . . .”¹⁹² Even when sellers commission extensive presale inspections for the benefit of prospective buyers, as sellers often do in high-end residential markets, brokers urge buyers to obtain their own inspections.

G. Should Sellers Be Required to Disclose Area-Wide Natural and Man-made Hazards?

Many forms ask sellers to disclose what they know about past flooding, seismic damage, and whether their properties are in a wetlands, form part of a coastal barrier against erosion, or possess other significant features bearing on the property’s use and development. Buyers who want to learn more than the seller about such matters must find out on their own.

In 1998, the California legislature went beyond asking sellers to disclose what they know when it enacted “the most comprehensive requirements of any state for disclosure of natural hazards to real estate.”¹⁹³ The California Natural Hazard Disclosure Law requires sellers and listing brokers to disclose whether the property is within a special flood hazard area designated by FEMA, a dam failure inundation area mapped by the State Office of Emergency Services, a seismic hazard zone as indicated by the State Geologist under the State Seismic Hazard Mapping Act, an official earthquake fault zone as indicated by the State Geologist, a very high fire-hazard severity zone according to state or local government maps, or a wildland forest fire-risk zone according to the California

¹⁹¹ See Mark R. Hinkston, *Residential Real Property Disclosure Duties*, WIS. LAW., May 2002, at 10, 50-51 (reviewing Wisconsin’s Home Inspector Act).

¹⁹² Weinberger, *supra* note 51, at 417-18.

¹⁹³ Hendricks, *supra* note 167, at 108.

Department of Forestry and Fire Protection.¹⁹⁴

The statute conditioned the obligation of sellers and listing brokers to provide this information on their possessing actual knowledge or a local agency making available maps showing parcels affected by the various hazards. In reality, sellers have difficulty ascertaining whether the local jurisdiction has such maps, and if it does, in obtaining them.¹⁹⁵ To remove any doubt about whether exempt sellers must provide natural hazard disclosures, the latest California Association of Realtors Residential Purchase Agreement obligates sellers to make natural hazard disclosures even if exempt.¹⁹⁶ Realtors have become proactive, anticipating that information about these hazards could be regarded by courts as material to buyers.

Certainly, if buyers find this information useful, it would be more cost effective for sellers, rather than buyers, to procure it. Because some buyers do not complete their sales, more than one prospective buyer may want to see the same report, making a single purchase by the seller more efficient. Also, large brokerage firms dominate the residential sales market and because of the high volume of reports they order, they have been able to negotiate favorable prices from information providers, a savings they could pass on to the seller.

Roughly seven out of ten natural hazard disclosures have one or more of the six statutory items marked "yes."¹⁹⁷ Evidence shows that some buyers regard this information as relevant. Mike Hull estimates that three to five percent of buyers invoke a negative natural hazard disclosure as a reason for cancellation.¹⁹⁸ A recent study of the consequences of this law shows that Hispanic buyers in flood plains paid, on average, \$4,220 less than they would have paid without the disclosure.¹⁹⁹

By reducing property values in flood plains, some legislators hoped

¹⁹⁴ See CAL. CIV. CODE § 1103 (West Supp. 2004).

¹⁹⁵ See Jeffrey G. Wagner, *Natural Hazard Disclosure*, CAL. B.J., Aug. 1999, at 10 ("The author, in a random and unscientific test of city and county agencies for information on hazard areas within their jurisdictions found the experience frustrating and futile. Inquiries were met with silence or 'Let me transfer you to another department.'").

¹⁹⁶ See CAL. ASS'N OF REALTORS, RESIDENTIAL PURCHASE AGREEMENT ¶ 5B (2002) (on file with the author).

¹⁹⁷ Telephone Interview with Sergio Siderman, *supra* note 141.

¹⁹⁸ Telephone Interview with Mike, *supra* note 86.

¹⁹⁹ See Austin Troy & Jeff Romm, *An Assessment of the California Natural Hazard Disclosure Law* (AB 1195) 15 (Feb. 11, 2003) (unpublished California Policy Research Center Report, subject to editorial changes) (cited with permission of authors), available at <http://www.uvm.edu/~atroy/CPRC-03.pdf>.

the law would marginally discourage flood plain development as developers factored lower sale prices into their pro formas for new development. The statute requires other important information to be brought to the attention of buyers in natural hazard areas, particularly the need for flood plain insurance, the added cost of brush clearance and vegetative maintenance in high fire-risk zones, and the possibility that local building codes might prohibit reconstruction in high hazard risk areas or impose costly new standards. Owners in California's high fire-risk areas are often able only to obtain insurance through a state-run program called the FAIR Plan (Fair Access to Insurance Requirements) through which all home insurers subsidize the premiums of residents in high fire-risk areas.²⁰⁰ Buyers are advised to talk with an insurance agent, starting with the seller's agent, as part of their due diligence effort.

So much for developing a case in favor of the statute. Much can be said against the statute as well.

Compliance with California's Natural Hazard Disclosure Law costs sellers money. Most sellers have no practical alternative other than to pay specialized firms \$50 to \$100 per transaction to provide the required information. Considering that the median California home sales price was \$376,000 in June 2003,²⁰¹ this may not seem like much money. But with estimated compliance rates of ninety percent or more and nearly 600,000 resales of existing homes (new home sales are exempt), California sellers are spending \$27,000,000 to \$54,000,000 a year for natural hazard disclosure reports.

Natural hazard disclosures lull some buyers into assuming that these reports can substitute for an on-site geology study, but nothing could be further from the truth. The consultants, who gather natural hazard data from public agencies and retail it through brokers to home sellers, do not visit the site and can offer none of the site-specific information a buyer would need to assess the site's suitability for the buyer's purposes.

The list of natural hazard items in the statute is incomplete and can mislead some sellers and brokers into believing they have fulfilled their legal disclosure obligation by divulging information about only the six listed items. In California, a property located outside any of the six areas mentioned in the statute could still be at great risk due to environmental hazards. The statute does not mention landslides, liquefaction, radon, local

²⁰⁰ See CAL. INS. CODE § 10090 (West 1993).

²⁰¹ See Press Release, California Association of Realtors, Sales Price Report (June 3, 2003) (on file with author).

fault activity, proximity to a nuclear power plant, areas where dangerous chemicals are stored or processed, ultramafic rock (naturally occurring asbestos zones), toxic landfills, or airport noise corridors.

Even before the revisions in the Civil Code, the larger brokerage firms were contracting for natural hazard disclosure information,²⁰² and the firms providing it included most of this information in their disclosures.

Since the enactment of the Natural Hazard Disclosure Law, twenty to thirty firms have gone into the business of gathering and retailing environmental hazard information, with varying degrees of accuracy. Most of the property disclosure firms formed after the enactment of the statute confine their reports to the six enumerated items in the statute. Some of the newly formed firms providing the natural hazard disclosure information rely on inappropriate mapping information, such as maps drawn at a scale far too large for accurate translation to the boundaries of individual parcels, maps that are out of date, and property address data showing each parcel as a dot instead of accurately depicting the boundaries of each property.²⁰³ These firms get away with sloppy mapping procedures and providing incomplete reports because the statute exonerates the expert from responsibility "for any items of information, or parts thereof, other than those expressly set forth in the statement."²⁰⁴ By statute, sellers and brokers also are immune from liability for errors and omissions in the reports they purchase.²⁰⁵

Much of the underlying data in any natural hazard disclosure is likely to be misleading because of the limited ability to predict when and where natural hazards, such as earthquakes, will occur. Geologists suspect that California is overdue for some major seismic activity in the next two hundred to one thousand years. In geologic time, this is a nanosecond. To geographers, the "recent past" refers to geologic events of 100,000 to

²⁰² Telephone Interview with Mike Hull, *supra* note 86.

²⁰³ Many firms rely on TIGER files, an extensive geographic data base developed by the U.S. Bureau of the Census and the U.S. Geological Survey. TIGER is an acronym for Topologically Integrated Geographically Encoded Referencing, an electronic street map integrating street addresses and census areas with features such as political boundaries, roads, railways, pipelines, streams, and shorelines. See MONMONIER, *supra* note 168, at 229. This data is adequate for finding driving directions because, after all, it was prepared for census takers looking for street addresses. But the data is insufficient for natural hazard disclosures because it does not map individual property boundaries, which is crucial for accurately determining whether property is within a flood plain, high fire-risk area, or within fifty feet of a surface earthquake fault. For these purposes, recorded subdivision maps or tax assessor data are superior.

²⁰⁴ CAL. CIV. CODE § 1103.4(c) (West Supp. 2004).

²⁰⁵ See CAL. CIV. CODE § 1103.4(a).

200,000 years ago.²⁰⁶ But few home buyers are thinking much beyond the next ten or fifteen years in making their acquisition decision, and most developers work on a two to seven year time horizon.

Fault line designations do not forecast the likely locus of earthquake damage very well. Seismic damage comes mostly from ground shaking and varies with the type of shaking, soil conditions, and construction methods. The worse damage often occurs many miles from any previously detected fault. One author noted that:

Whether Californians have learned much from two decades of fault-zone mapping is questionable. . . . The 1994 earthquake that killed fifty-six people in and around Northridge and caused more than \$15 billion in damage to buildings, highways, and personal property demonstrates the folly of hazard-mitigation planning focused largely on surface faults. . . . The earthquake that devastated Northridge originated far below the surface on an unknown fault.²⁰⁷

FEMA maps flood hazard zones in connection with the National Flood Insurance Program. The data purports to pinpoint the location of the one hundred year flood plain and one hundred year coastal flood plain—areas adjoining a natural body of water predicted to have a one percent chance of being inundated each year by overflows in heavy rainfall. Federally regulated lenders are required to give homeowners of properties located in certain designated flood hazard areas notice of the danger and require them to purchase national flood insurance.²⁰⁸

Because FEMA does not delineate the precise boundaries of the properties mapped, their maps are not ideal for determining whether any particular property lies within a flood plain. Inaccuracies—and FEMA maps are notoriously inaccurate—are not fatal to FEMA's setting flood insurance premiums because premiums not collected from *A*, whose property was erroneously excluded from the flood plain, may be collected instead from *B*, whose property was mistakenly included. But those errors can be worrisome to sellers of properties incorrectly described as being within the flood plain and equally disappointing to unlucky buyers purchasing parcels wrongly described as falling outside the flood plain and

²⁰⁶ Interview with Dr. Jim Dolan, Associate Professor of Earth Sciences, University of Southern California, in Los Angeles, Cal. (July 1, 2003).

²⁰⁷ MONMONIER, *supra* note 168, at 25.

²⁰⁸ See 42 U.S.C. § 4013(a) (2000).

later reclassified as flood prone.

Even when the flood plain mapping is accurate, its usefulness is diminished by the inability to predict when a so-called one hundred year flood will occur. In reality, there could be one hundred year floods in several consecutive years followed by none for generations.²⁰⁹ The fact that last year was dry is no indicator of what this year's weather will bring, no more than one could safely predict that a flipped coin, after landing "tails," will land "heads" on the next throw. Because these are indicators of low probability, high risk events, most buyers discount the data anyway except for hazards that have occurred recently. Then, buyers overestimate the chances of recurrence.²¹⁰

Some of the data called for in California's Natural Hazard Disclosure Law can be misleading because of political manipulation. Local governments and property owners do not want to stigmatize their area as unsafe. So, over half the cities in California that the state regarded as containing high fire-risk areas were able to remove their jurisdictions from the state high fire-risk maps. Among those that succeeded in exempting themselves is Oakland Hills, a hillside, high-income residential area and the site of one of California's worst fires, a 1991 blaze resulting in \$1.9 billion in damage. Ironically, the devastating Oakland Hills fire prompted the statewide program of mapping high fire-risk areas.

To Californians, nothing illustrates the limited value of the natural hazard disclosure better than the realization that a buyer in Northridge before the devastating 1994 earthquake would not have been forewarned of any potential seismic risk. Nor would the statute require that an Oakland Hills purchaser today be told that the fire leveled the area just over a decade ago.²¹¹

Generally, buyers report that the natural hazard disclosures made no difference in their decision whether to go through with the sale or in setting their purchase price (with the one exception noted earlier for Hispanics buying into low-income neighborhoods located in flood plains). This result is not surprising. Most southern Californians know "California

²⁰⁹ Interview with John P. Wilson, Professor of Geography and Director, G.I.S. Laboratory, University of Southern California, in Los Angeles, Cal. (June 25, 2003).

²¹⁰ See Daniel Kahneman & Amos Tversky, *Prospect Theory: An Analysis of Decision Under Risk*, in CHOICES, VALUES, AND FRAMES 17, 22-25 (Daniel Kahneman & Amos Tversky eds., 2000).

²¹¹ In their standard disclosures, most Realtors in the area note the Oakland fire or the possibility of one. E-mail from Victoria B. Naidorf to George Lefcoe, *supra* note 101.

rests on a web of geographic faults.”²¹² Southern California is “home to half of all the earthquake risks in the United States.”²¹³ Buyers realize they are purchasing flood prone property when they pay a premium for sites directly fronting on a river, lake, or ocean. Similarly, high fire-risk areas—wooded hillsides and bucolic rural settings—are among the most treasured residential locations in California. Because most buyers are aware of flood and fire risks and are no less capable than sellers of assessing these risks, some courts have freed sellers of any obligation to disclose natural hazard conditions.²¹⁴

Regarding these hazard issues, one scholar noted:

All parts of the country, even deserts, are subject to flooding, so that instead of a belt, the nation’s streams, rivers, and coastlines blanket the country with a dense network of narrow flood hazard zones. . . . Because of its lattice-like geography, flood damage can usually be reduced, if not avoided altogether, by moving back from the water’s edge toward higher ground. But persuading people to retreat is difficult; relocating structures is expensive, and flood-prone areas offer aesthetic amenities that other hazards lack—unlike toxic waste sites, for example, it’s delightful to have a home and property where “a river runs through it.”²¹⁵

Buyers can be informed about natural hazards in ways less costly than the one California has chosen. For example, Hawaii legislated natural hazard disclosures comparable to those required in California. But instead of burdening home sellers with gathering information piecemeal from numerous public agencies or paying private firms to accumulate the data, the legislature conditioned compliance on counties’ first obtaining the relevant maps and making them publicly available at a reasonable copying

²¹² Troy & Romm, *supra* note 199, at 16-20 (“Based on these results it appears that fire disclosure had no effect for the overall population of fire zone houses. . . . The amenity value . . . was strong enough, and the floodplain premium weak enough that the two cancelled each other out.”).

²¹³ Eva Emerson, *SCEC Scientists Cross Boundaries to Better Understand Earthquakes in L.A. and Beyond*, U.S. CAL. C. OF LETTERS, ARTS & SCI., Summer 2003, at 10 (quoting Tom Jordan, W.M. Keck Foundation Chair in Geological Sciences at USC College).

²¹⁴ See *Nelson v. Wings*, 699 So. 2d 258, 260 (Fla. App. 1997) (holding that sellers had no duty to disclose that East Everglades was subject to flooding, especially because the house was elevated and provided visual evidence of local code requirements imposed to minimize flood damage).

²¹⁵ MONMONIER, *supra* note 168, at 105-06.

fee.²¹⁶ No Hawaii county has yet met the condition, so sellers do not bother trying to comply with the statute. Still, according to counsel for the Hawaii Association of Realtors, no buyers have complained.²¹⁷

If the legislature believes buyers need this information, states could fund more generously the state and local agencies already engaged in mapping natural hazards, instead of requiring home sellers spend tens of millions of dollars annually on natural hazard disclosures.²¹⁸ Then, sellers and brokers could supply buyers with a list of government websites, leaving buyers to decide how much time to spend browsing the web.

Even now, homeowners and prospective buyers can access the website of the California state geological survey for maps of earthquake faults, landslides, ultramafic rock, and other hazards.²¹⁹ A few local governments in California are currently providing all of the maps needed to determine whether a property lies within one of the six types of areas delineated in the Natural Hazard Disclosure Law. Buyers in these jurisdictions could be referred to the place where the maps are kept. In Oahu, Hawaii, the telephone book contains a map depicting low lying areas from which residents should flee in a tsunami condition.²²⁰

²¹⁶ See HAW. REV. STAT. ANN. § 508D-15 (Michie 2001).

²¹⁷ Telephone Interview by Robert Cooper with Wayne Pitluck, Counsel, Hawaii Association of Realtors (Aug. 7, 2003).

²¹⁸ The legislature seems well aware of the need for state agencies to design uniform, usable maps depicting the various natural hazards.

The Legislature finds and declares that city and county planning agencies sometimes have difficulty using the maps and information produced by state departments and agencies regarding natural hazards because the maps may be at different scales, use different projections, or are otherwise incompatible. The Legislature finds and declares that the lack of compatible maps sometimes makes it difficult for city and county planning agencies to make information regarding natural hazards readily available to landowners, their agents, and the public. Therefore, the Legislature finds and declares that there is a need for state officials to coordinate their natural hazard mapping and information programs to make them more effective. The Legislature encourages the Secretary of the Resources Agency to provide coordination and leadership among the state departments and agencies. . . .

CAL. CIV. CODE § 1102.6c note (West Supp. 2004) (Historical and Statutory Notes) (repealed 1999).

²¹⁹ See Steven Tafoya Naumchik, *Seller Beware: More Hazard Disclosure Requirements in the Sale of Real Property*, 30 MCGEORGE L. REV. 713, 721 (1999) ("Unfortunately, [the Natural Hazard Disclosure Act] recognizes the State of California's lack of uniform or compatible hazard area maps, which vary by agency, but institutes no plan for coordinating them.").

²²⁰ See MONMONIER, *supra* note 168, at 65.

In areas mapped for coastal erosion, New York offers a cost effective solution to one special, natural hazard disclosure problem. The New York Department of Environmental Conservation maps critical erosion areas, notifies affected owners individually, and gives the owners a chance to protest before the map becomes final.²²¹ Once personally notified, sellers are legally bound to relay this information to prospective buyers.

Another way to lighten disclosure burdens on sellers would be to follow the New Jersey model. A controversial New Jersey court opinion held homebuilders liable for failing to disclose that a toxic landfill was located half a mile from the site of newly built homes when they marketed the site as being in a healthful, bucolic setting.²²² To free homebuilders of this disclosure burden, the New Jersey legislature instructed the Commissioner of Environmental Protection to inform localities of sites where hazardous discharges had occurred and mandated municipalities to make this information available to the public. At the time of contracting, sellers of newly constructed homes are now required to notify purchasers of the address and phone number of the municipal clerk.²²³ After receiving notification, purchasers have five days to cancel their purchase contracts.²²⁴

Many natural hazards could be satisfactorily described in a pamphlet provided to buyers. Some local Realtors associations prepare and issue pamphlets for their members to give prospective buyers informing them of local environmental concerns within their jurisdictions.²²⁵ For instance, the San Francisco Association of Realtors prepared a thirty-one page booklet covering such topics as air traffic, rent control, financing, authorized use of property, code compliance, and "various other state and local laws that impact the purchase or sale of property."²²⁶ Preparing region-wide natural hazard disclosure brochures, which could include the FEMA and state geologist maps, would be less costly than putting every seller in the position of purchasing this information from a private firm.

²²¹ See N.Y. ENVT'L. CONSERV. LAW § 34-0101, -0102, -0104 (McKinney 1997).

²²² See *Strawn v. Canuso*, 657 A.2d 420, 431 (N.J. 1995).

²²³ See N.J. STAT. ANN. § 46:3C-8 (West 2003).

²²⁴ See *id.*

²²⁵ Property I.D. Corporation supplies this information, but other natural hazard disclosure firms do not. See PROPERTY I.D. CORP., A SPECIAL REPORT ON NATURAL HAZARD DISCLOSURE: MAKING SMART DECISIONS ON AN UNREGULATED PRODUCT (undated) (on file with author).

²²⁶ Letter from Victoria B. Naidorf *supra* note 133.

VII. CONCLUSION

Common-law courts changed the law of seller disclosure from *caveat emptor* to "seller tell all." This amorphous, court-imposed disclosure requirement invited fact-laden trials with unpredictable outcomes, as litigators wrestled over what information was material, latent, known to the seller, and inaccessible to the buyer.

Courts then began holding brokers jointly and severally accountable to buyers who were injured by seller misrepresentations. To cut back on their own expanding liability, to assist buyers to become fully informed about a property before committing to a purchase, and to clarify for sellers exactly what they should disclose, Realtors developed a disclosure protocol now in place throughout the country. Sellers are given no practical choice but to fill out a detailed property condition disclosure form for the benefit of prospective buyers. As the Realtors anticipated, buyers who receive these reports are less likely to be disappointed with their home purchases afterward, and are also less likely to file insurance claims and lawsuits against sellers or brokers for undisclosed defects.

Realtors have assumed the primary responsibility for revising disclosure questionnaires to keep current with evolving buyer concerns, court decisions, and new laws and regulations. Realtors translate sometimes confusing and obscure norms into simple "yes" or "no" questions that sellers answer in completing disclosure forms. In this way, the real estate industry has eased the transition from *caveat emptor* to "seller tell all."