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## Violations of Zoning Ordinances, the Covenant Against Encumbrances, and Marketability of Title: How Purchasers Can Be Better Protected

Cover Page Footnote

23-1

# **VIOLATIONS OF ZONING ORDINANCES, THE COVENANT AGAINST ENCUMBRANCES, AND MARKETABILITY OF TITLE: HOW PURCHASERS CAN BE BETTER PROTECTED**

*Jessica P. Wilde\**

## **I. INTRODUCTION**

Zoning ordinances function as an exercise of the government's general police power, sustaining the enjoyment, health, and safety of the public. They are important in order to maintain property values and protect a neighborhood's quality and environment.<sup>1</sup> Zoning ordinances prevent people from using their property in a way that would make a neighborhood less enjoyable.<sup>2</sup> State statutes often provide civil and criminal penalties for failing to comply with zoning ordinances.<sup>3</sup> Noncompliance with existing ordinances may be of concern to a buyer who buys a parcel of land

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<sup>1</sup> See ROBERT H. NELSON, ZONING AND PROPERTY RIGHTS: AN ANALYSIS OF THE AMERICAN SYSTEM OF LAND USE REGULATION 11-12 (1977).

<sup>2</sup> *Id.* They are often enacted for safety purposes; for example, a zoning ordinance prevents commercial use in a residential neighborhood or may require a permit or certificate of occupancy before a building is occupied. In addition, a zoning ordinance may be in the form of a building code, requiring that the building maintain certain requirements for fire code purposes. Ordinances serve an array of important functions in order to maintain the value and enjoyment of a neighborhood, as well as facilitate the safety and health of the public.

<sup>3</sup> Adam Forman, Comment, *What You Can't See Can Hurt You: Do Latent Violations of a Restrictive Land Use Ordinance, Existing Upon Conveyance, Constitute a Breach of the Covenant Against Encumbrances?* 64 ALB. L. REV. 803, 806 (2000) (discussing latent violations with respect to the covenant against encumbrances and how purchasers can seek to protect themselves).

unaware that the use of the property violates an ordinance. A buyer, upon discovering a violation prior to closing, may want to rescind the contract. Similarly, a buyer may be frustrated if he or she discovers a violation when trying to sell the property at a later date, making the property difficult to sell. Also, perhaps a subsequent purchaser seeks to make a change to the property, discovers a violation, and then must pay a substantial amount of money to fix the defect. When one discovers a violation, what often emerges is the crossroad between zoning ordinances and the covenant against encumbrances in a general warranty deed, as well as the contract guarantee to convey marketable title.

A covenant against encumbrances is a present covenant.<sup>4</sup> When an encumbrance exists at the time of conveyance, there is a defect on the title and the grantor has breached the covenant against encumbrances. If a subsequent purchaser discovers a violation after the deed has been granted and his possession is disturbed or he has to pay off the encumbrance, he may hold the grantor liable and receive nominal damages.<sup>5</sup> However, if a purchaser discovers a violation of a zoning ordinance prior to the conveyance, then he may seek to rescind the contract prior to closing on the theory that the seller would be conveying unmarketable title due to the existing violation.<sup>6</sup>

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<sup>4</sup> 20 AM. JUR. 2D *Covenants, Conditions, and Restrictions* § 89 (2004). Encumbrances may include violations of zoning ordinances, as well as mortgages, liens, easements, and covenants. An encumbrance has also been defined as “every right to, or interest in, the land, to the diminution in value of the estate, but consistent with the passage of the fee by the conveyance.” *Id.* § 87.

<sup>5</sup> *Id.* § 131.

<sup>6</sup> However, a seller may be afforded the opportunity to remove the encumbrance within a reasonable amount of time so that he can convey title that is free and clear from encumbrances. 77 AM. JUR. 2D *Vendor and Purchaser* § 86 (2004). See also Pamerqua

Marketable title<sup>7</sup> is title free from reasonable doubt in which a reasonable person would not hesitate to purchase the property.<sup>8</sup> Marketable title guarantees that property is “free and clear of encumbrances.” Furthermore, “ ‘encumbrances’ includes [sic] any right to or interest in the land subsisting in another to the diminution of its value.’ ”<sup>9</sup> Marketable title is a typical contract provision for real estate sales, and is presumed when absent from the contract.<sup>10</sup> A purchaser, upon discovering a violation prior to closing, might seek rescission based upon breach of contract.

Claims by a purchaser brought against a seller for violations of ordinances may therefore arise in the form of either the failure to convey marketable title or the breach of the warranty against encumbrances. These two remedies, although the former based in contract and the latter based on a general warranty deed, are similar in substance.<sup>11</sup> When a purchaser discovers a violation and is deciding what claim to bring, the answer is based largely on timing. Additionally, courts find that unmarketable title exists when there is

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*Realty Corp. v. Dollar Serv. Corp.*, 461 N.Y.S.2d 393, 395 (App. Div. 1983) (“[W]here it reasonably appears that the vendee will be plagued by zoning problems when he purchases the property, a title defect does exist and the vendee is entitled to demand that the vendor rectify the same or return any moneys paid on account.”).

<sup>7</sup> See *infra* notes 41-42 and accompanying text.

<sup>8</sup> See *Vendor and Purchaser*, *supra* note 6, § 105.

<sup>9</sup> *Id.* § 147.

<sup>10</sup> *Voorheesville Rod & Gun Club, Inc. v. E.W. Tompkins Co.*, 626 N.E.2d 917, 920 (N.Y. 1993) (“[I]n the absence of a stipulation to the contrary, it is presumed that a marketable title is to be conveyed.”).

<sup>11</sup> A primary difference between the two is that the contractual guarantee to convey marketable title is made when the contract is signed and ceases at the time of conveyance. A purchaser who, prior to closing, discovers a violation, may seek to rescind the contract because the seller would be unable to convey marketable title. On the other hand, the seller warrants that there are no encumbrances affecting title when the deed is conveyed. A purchaser who, subsequent to closing, discovers a violation, may seek to bring a claim based upon the covenant.

an existing encumbrance.<sup>12</sup> The promise to convey marketable title and the warranty that there are no encumbrances on the title are closely related, therefore they will be discussed together.

Although the contract and warranty creates remedies that seek to protect a buyer, unfortunately, in many instances, the buyer is left unprotected. The longstanding common law doctrine of caveat emptor, or “buyer beware,” led to the use of covenants so buyers could protect themselves.<sup>13</sup> While most states have departed from the caveat emptor rule, sellers often do not have the duty to make representations to the buyer concerning violations of restrictions and ordinances.<sup>14</sup> Some states continue to adhere to the caveat emptor rule, in which the seller does not have the duty to make representations to the buyer concerning the property.<sup>15</sup> The purchaser has the responsibility for determining whether the existing land uses comply with municipal ordinances by inspecting the property and by seeking a title report. The seller does not have to disclose violations, whether they are material or latent, and does not have to make any representations about the continued use of the land.<sup>16</sup>

Misrepresentation law also leaves gaps that result in a failure

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<sup>12</sup> The standard contract provision states that the sellers shall convey marketable title, free and clear of all encumbrances except for those certain ones that are specified. *See Vendor and Purchaser*, *supra* note 6, § 147.

<sup>13</sup> 67 AM. JUR. 2D *Sales* § 638; *see Colonial Capital Corp. v. Smith*, 367 So. 2d 490, 492 (Ala. Civ. App. 1979) (“The doctrine of caveat emptor generally is applicable to the sale of real estate in this state. Except in cases of fraud, the only protection of title afforded a purchaser is the covenants contained in the deed.”).

<sup>14</sup> Eric T. Freyfogle, *Real Estate Sales and the New Implied Warranty of Lawful Use*, 71 CORNELL L. REV. 1, 2 (1985).

<sup>15</sup> *See infra* Part IV.B.

<sup>16</sup> Freyfogle, *supra* note 14, at 1.

to protect an innocent purchaser.<sup>17</sup> The duty to discover violations is largely placed on the buyer. Yet many violations are difficult to discover, even after obtaining a title report from a title insurance company. The difficulty arises largely from the lack of reliable and consistent municipal records. Many courts have held that violations of ordinances that are hidden, unknown or latent are not encumbrances within the scope of the covenant.<sup>18</sup> Furthermore, courts have held that latent violations of ordinances have no effect on marketable title, leaving a buyer without the ability to rescind the contract.<sup>19</sup>

This Comment discusses the types of violations that have not been encompassed within the covenant against encumbrances or the scope of the marketable title guarantee, and how purchasers can be better protected. Part II discusses the case law history involving the development of the covenant against encumbrances and the guarantee to convey marketable title.<sup>20</sup> Part III evaluates examples of violations of ordinances that have not been encompassed within the covenant against encumbrances and marketable title, thereby creating an exception to the general rule.<sup>21</sup> Then, Part IV explores the duties on buyers and sellers with respect to disclosure and discovery of violations. Part IV also discusses the caveat emptor doctrine and how it implicates the duty on sellers to make disclosures about the lawful

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<sup>17</sup> *Id.* at 5-16 (discussing misrepresentation law and the difficulty in applying it in instances where there have been violations of ordinances).

<sup>18</sup> *See infra* Part III.A (discussing building code violations).

<sup>19</sup> *See infra* Part III.B (discussing latent violations).

<sup>20</sup> *See infra* Part II.

<sup>21</sup> *See infra* Part III.

use of their property.<sup>22</sup> In addition, Part IV introduces the implications of title insurance companies and their duties. Finally, Part V will explore what can be done in the future to better protect purchasers.<sup>23</sup> Specifically, purchasers should be aware that in many jurisdictions a seller has no duty to disclose violations of ordinances and regulations, and that purchasers should seek warranties or promises to disclose from sellers.<sup>24</sup> Also, an implied warranty of lawful use should be implemented so purchaser can be better protected.<sup>25</sup>

This Comment concludes that there is a need in the area of property law for purchasers of real estate to be better protected when the land purchased is in violation of ordinances or regulations. Today, purchasers carry a heavy burden even though sellers are often in a better position to have more knowledge of existing violations. Although courts have showed sympathy to unprotected buyers,<sup>26</sup> the trend among the courts to narrow the scope of the covenant against encumbrances and the contract to convey marketable title places buyers at a loss. The covenant and scope of marketable title must not be sliced away, leaving purchasers unprotected. Furthermore, sellers should have a higher duty placed on them to warrant the existing use of their property and any violations thereof. An implied warranty of lawful use is a potential avenue for recovery.<sup>27</sup>

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<sup>22</sup> See *infra* Parts IV.A-B.

<sup>23</sup> See *infra* Part V.

<sup>24</sup> See *infra* Part V.A.

<sup>25</sup> See *infra* Part V.B.

<sup>26</sup> This is shown by the departure from the caveat emptor rule.

<sup>27</sup> See *infra* Part V.B.

## II.      **THE DEVELOPMENT OF THE COVENANT AGAINST ENCUMBRANCES AND MARKETABLE TITLE IN CASE LAW**

Part II will discuss, as developed through extensive case law, how zoning ordinances affect title, beginning with the “grand daddy” case of *Lincoln Trust Co. v. Williams Building Corp.*<sup>28</sup> The majority rule that a mere zoning ordinance does not constitute an encumbrance, but a *violation* of a zoning ordinance does constitute an encumbrance for the purposes of marketable title and the covenant against encumbrances, will be explained. Cases holding that a violation of a zoning ordinance constitutes an encumbrance will be discussed in section A.<sup>29</sup> Section B will discuss a jurisdiction that has departed from the general rule.<sup>30</sup> Finally, Part II will provide the framework for how basic violations of zoning ordinances affect title and the covenant against encumbrances.

*Lincoln Trust*, a New York Court of Appeals decision, is one of the leading cases on zoning ordinances and its effect on title. A vendee contracted for the sale of certain real estate in New York City, which was to be conveyed “free from all encumbrances.”<sup>31</sup> Yet, a zoning law restricting the use for residential purposes had been passed a month prior to the date of contract.<sup>32</sup> The defendant purchaser sought to rescind the contract so the plaintiff brought an action for specific performance.<sup>33</sup> The court granted specific

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<sup>28</sup> 128 N.E. 209 (N.Y. 1920).

<sup>29</sup> See *infra* Part II.A.

<sup>30</sup> See *infra* Part II.B.

<sup>31</sup> *Lincoln Trust*, 128 N.E. at 209 (quotation omitted).

<sup>32</sup> *Id.* at 209-10.

<sup>33</sup> *Id.* at 209.

performance and in reaching its decision, held that municipalities must make certain resolutions and consider the “public health, welfare, convenience and common good” in exercising its police power.<sup>34</sup> The court found that courts should not interfere with the exercise of the police power,<sup>35</sup> which includes the regulation of the use of property.<sup>36</sup>

The impact of *Lincoln Trust* is “that where a person agrees to purchase real estate, which, at the time, is restricted by laws [and] ordinances, he will be deemed to have entered into the contract subject to the same.”<sup>37</sup> In other words, an ordinance on its face does not constitute an encumbrance.<sup>38</sup> In comparison, easements and private covenants do constitute encumbrances.<sup>39</sup> This is perhaps due to the fact that in a private covenant, the entity being benefited is a private landowner, as opposed to a governmental entity.<sup>40</sup>

Although municipal, state, and governmental ordinances on their face do not constitute encumbrances, the question of whether a *violation* of such an ordinance constitutes an encumbrance does arise. In other words, does a violation of an ordinance breach the covenant

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<sup>34</sup> *Id.* at 210.

<sup>35</sup> The court lists numerous examples of when a municipality has been able to limit and prohibit the use of certain property. *See id.*

<sup>36</sup> *Lincoln Trust*, 128 N.E. at 209-10 (citing *Hauser v. No. British & M. Ins. Co.*, 100 N.E. 52 (N.Y. 1912)).

<sup>37</sup> *Id.* at 210.

<sup>38</sup> *See generally* George P. Stephan, Comment, *Public Land Use Regulations and Marketability of Title*, 1958 WIS. L. REV. 128 (1958).

<sup>39</sup> *See generally* Allison Dunham, *Effect on Title of Violations of Building Covenants and Zoning Ordinances*, 27 ROCKY MTN. L. REV. 255 (1955).

<sup>40</sup> *See Chesebro v. Moers*, 134 N.E. 842 (N.Y. 1922). Furthermore, when a landowner subdivides parcels with a restriction imposed upon conveyance, it has previously been held that negative easements were created. *See id.* at 843. This history might provide an explanation why covenants on their face constitute encumbrances.

in a deed against encumbrances? Additionally, does a violation of an ordinance render title unmarketable, such that a purchaser may rescind the contract prior to closing?

**A. Cases Finding Title Unmarketable or a Breach of the Covenant Against Encumbrances Where the Property Violates an Ordinance**

The cases discussed in this section hold that a breach of a zoning ordinance renders title unmarketable and is a violation of the covenant against encumbrances. Unmarketable title is title “that a reasonable buyer would refuse to accept because of possible conflicting interests in or litigation over the property.”<sup>41</sup> A buyer should not be forced to take title that is subject to doubt, and title is doubtful when it exposes one to litigation.<sup>42</sup> Unlike the covenant against encumbrances, in a suit alleging unmarketable title, only private covenants and violations of zoning ordinances are encumbrances. Sellers have the opportunity up until the time of closing to remedy a lien or an existing mortgage (which is usually satisfied at closing).<sup>43</sup>

In *Moyer v. DeVincentis Construction Co.*,<sup>44</sup> a case decided thirteen years after *Lincoln Trust*, the Pennsylvania Supreme Court held that a violation of a zoning ordinance rendered the title

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<sup>41</sup> BLACK’S LAW DICTIONARY 711 (2d pocket ed. 2001).

<sup>42</sup> *Speakman v. Forepaugh*, 44 Pa. 363, 371 (1863); *see also* 1 JOSEPH RASCH, NEW YORK LAW AND PRACTICE OF REAL PROPERTY § 22:1 (2d ed. 1991) (describing marketable title as “merely one that is free from encumbrances and free from reasonable doubt as to any fact or point of law upon which its validity depends”).

<sup>43</sup> *See supra* note 6.

<sup>44</sup> 164 A. 111 (Pa. 1933).

unmarketable.<sup>45</sup> After contracting to purchase a home, the plaintiff learned that an existing encroachment violated a zoning ordinance.<sup>46</sup> The ordinance stated that if there was a violation, “appropriate proceedings may be had to prevent the occupancy of the building and prevent the illegal construction, maintenance or use.”<sup>47</sup> This validated the court’s position that such ramifications would perhaps expose the purchaser to subsequent litigation. Equally important was the court’s characterization of this encroachment as “substantial.”<sup>48</sup> The court apparently inquired into the severity of the violation in determining whether it will subject one to litigation.

Many courts agree with *Moyer* and have held that a violation of an ordinance renders title unmarketable. In 1951, the Supreme Court of Kansas, in *Lohmeyer v. Bower*,<sup>49</sup> held that the violations of an ordinance and a restriction encumbered the title as to “expose the party holding it to the hazard of litigation and make such title doubtful and unmarketable.”<sup>50</sup> A seller agreed to purchase a lot and later found out that the house was in violation of a city ordinance that required buildings to be erected not more than three feet from the side or rear of the lot.<sup>51</sup> The home was standing eighteen inches from the

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<sup>45</sup> *Id.* at 112.

<sup>46</sup> The zoning “ordinance required the building to be set back at least twenty-five feet from the street when it was, in fact, set back only twenty-two feet . . .” *Id.* at 111.

<sup>47</sup> *Id.* at 111.

<sup>48</sup> “Any *substantial* encroachment of a building upon adjoining land of a private owner or the public renders the title to the land on which the building is located unmarketable . . .” *Id.* at 112.

<sup>49</sup> 227 P.2d 102 (Kan. 1951).

<sup>50</sup> *Id.* at 110.

<sup>51</sup> *Id.* at 104.

boundary of the lot.<sup>52</sup> Furthermore, there was a violation of the restriction requiring a two-story house.<sup>53</sup> The *Lohmeyer* court explained that the mere existence of the ordinance did not constitute an encumbrance; yet, a violation of the ordinance did.<sup>54</sup> Although the contract excepted the restrictions of record, “it is the violation of the restrictions imposed by both the ordinance and the dedication declaration, not the existence of those restrictions, that renders the title unmarketable.”<sup>55</sup>

Similarly, in *Hartman v. Rizzuto*,<sup>56</sup> Hartman owned two lots and his application was accepted so he could build a duplex on the front half of one of the lots.<sup>57</sup> Then Hartman entered into a contract to sell the rear half of the lot.<sup>58</sup> It provided that they enter into an agreement whereby the “ ‘title to said premises is to be shown free and clear of incumbrances [sic]’ ” and “if title ‘shall not prove marketable’ and seller not be able to perfect the same within 90 days, ‘the purchaser shall have the option of . . . receiving back said deposit and shall be released from all obligations hereunder.’ ”<sup>59</sup> A city ordinance required the building to have a rear yard space of twenty-five feet, which included most of the distance of the rear half of the

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<sup>52</sup> *Id.*

<sup>53</sup> This was a Berkeley Hills Addition covenant and for our purposes, is not relevant. A covenant does not need to be violated in order to constitute an encumbrance. See Dunham, *supra* note 39, at 256 (“[I]t is immaterial whether the existing structure conforms to or violates the covenant; in either event the covenant is a defect in title.”).

<sup>54</sup> *Lohmeyer*, 227 P.2d at 108.

<sup>55</sup> *Id.* at 110.

<sup>56</sup> 266 P.2d 539 (Cal. Ct. App. 1954).

<sup>57</sup> *Id.* at 540.

<sup>58</sup> *Id.* at 540-41.

<sup>59</sup> *Id.* at 541.

lot.<sup>60</sup> The buyer sought his deposit and the seller instituted the action to recover the money; the buyer cross-complained seeking rescission.<sup>61</sup> The appellate court affirmed the trial court's granting of rescission.<sup>62</sup> The court explained that the piece of land was of no use to the buyers and all they would be able to do was to resell the property and explain to prospective buyers that the lot could not be used for a building.<sup>63</sup> In comparison to *Moyer*,<sup>64</sup> the *Hartman* court stated that the restrictions "substantially interfere with many uses which an owner reasonably might wish to make of the property . . . ."<sup>65</sup> Thus, both courts considered the materiality of the violation.<sup>66</sup>

Also, in *Oatis v. Decluze*<sup>67</sup> and *Wilcox v. Pioneer Homes, Inc.*,<sup>68</sup> the Louisiana and North Carolina courts held that a violation of an ordinance constituted an encumbrance and rendered the title unmarketable.<sup>69</sup> In *Oatis*, the property was zoned "residential" under a New Orleans ordinance, although the building constructed upon it contained three apartments, thus constituting a violation.<sup>70</sup> At issue in *Wilcox* was a city ordinance that required a minimum side lot of fifteen feet, although the house was slightly over three feet from the

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<sup>60</sup> *Id.* at 540.

<sup>61</sup> *Hartman*, 266 P.2d at 541.

<sup>62</sup> *Id.*

<sup>63</sup> *Id.*

<sup>64</sup> See *supra* notes 44-48 and accompanying text.

<sup>65</sup> *Hartman*, 266 P.2d at 541.

<sup>66</sup> *Id.* at 542 (stating that the violations were "deemed material").

<sup>67</sup> 77 So. 2d 28 (La. 1954).

<sup>68</sup> 254 S.E.2d 214 (N.C. Ct. App. 1979).

<sup>69</sup> *Oatis*, 77 So. 2d at 30; *Wilcox*, 254 S.E. 2d at 216.

<sup>70</sup> *Oatis*, 77 So. 2d at 29. The issue in the case turned on whether the apartments were constructed prior to or subsequent to the adoption of the ordinance. If they were erected after the adopted, this resulted in a violation that affects the title. *Id.* at 30.

property line.<sup>71</sup> The court held that the violation discovered post-closing constituted an encumbrance within the meaning of the warranty.<sup>72</sup> Generally, courts find violations of ordinances to breach the covenant against encumbrances, as well as render title unmarketable.<sup>73</sup>

**B.      A Deviation From the Majority Rule: Georgia's Holding That an Ordinance Violation Does Not Constitute an Encumbrance**

The State of Georgia has deviated from the general rule that violations of ordinances constitute an encumbrance. The Supreme Court of Georgia decided a case in 1991, *Barnett v. Decatur*,<sup>74</sup> which has received a great deal of attention in this area of the law. The Decatur's purchased a one-acre piece of property and subsequently discovered that the lot was in violation of the Fayette County ordinance that requires lots to have a minimum size of five acres.<sup>75</sup> The Decatur's sued the seller for the purchase price.<sup>76</sup> The Supreme Court of Georgia, reversing the court of appeals, held that the

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<sup>71</sup> *Wilcox*, 254 S.E.2d at 214. This was also in violation of a restrictive covenant that provided "no structure shall be located less than 7 feet from the side lines of the lot." *Id.*

<sup>72</sup> *Id.* at 216.

<sup>73</sup> See *Venisek v. Draski*, 150 N.W.2d 347 (Wis. 1967) (finding an ordinance requiring 120-foot frontage was violated and enforcing the contract would result in an illegal act); *Smith v. Pearmain*, 548 P.2d 1269 (Utah 1976) (finding a duplex in violation of existing ordinance). Cf. *Moss v. Rubenstein*, 191 N.Y.S. 496 (Sup. Ct. 1921) (finding a garage unusable under the existing ordinance).

<sup>74</sup> 403 S.E.2d 46 (Ga. 1991).

<sup>75</sup> *Decatur v. Barnett*, 398 S.E.2d 706, 707 (Ga. Ct. App. 1990). The lot was originally part of a larger parcel. A remote grantor subdivided it and the one-acre lot was sold to the plaintiff's grantors. The grantors sold the property to Caitlin Decatur, who conveyed it jointly to herself and her husband. *Id.*

<sup>76</sup> *Id.*

warranty of title does not include zoning matters.<sup>77</sup> The court relied on *Sachs v. Swartz*,<sup>78</sup> another Georgia decision, which stated that buyers and sellers are both presumed to know the zoning regulations when entering into a contract for sale.<sup>79</sup> The court in *Barnett* said that in *Sachs*, the zoning status of the property did not affect title.<sup>80</sup> *Barnett* suggests that a buyer has the duty to discover whether the property he or she is about to purchase is in violation of any zoning ordinances. What is surprising about this decision is that it was by no means a minor violation such as a building code violation.<sup>81</sup> The entire parcel was in violation, yet the Supreme Court of Georgia did not find that the one-acre lot constituted an encumbrance.<sup>82</sup>

*Barnett*, however, is a deviation from the general rule that violations of zoning ordinances constitute encumbrances. Unlike the *Oatis*<sup>83</sup> court and others,<sup>84</sup> *Barnett* is an exception. *Barnett* leads us to Part III, where more generally accepted exclusions to the rule that violations constitute encumbrances will be discussed. Although the majority of jurisdictions find violations of ordinances to be encompassed within the scope of the covenant against encumbrances, courts in some jurisdictions hold that there are certain types of

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<sup>77</sup> *Barnett*, 403 S.E.2d at 47.

<sup>78</sup> 209 S.E.2d 642 (Ga. 1974); see *Barnett*, 403 S.E.2d at 47.

<sup>79</sup> *Sachs*, 209 S.E.2d, at 645.

<sup>80</sup> *Barnett*, 403 S.E.2d at 47.

<sup>81</sup> See *infra* Part III.A. Building code violations are generally not encumbrances within the scope of the covenant.

<sup>82</sup> *Barnett*, 403 S.E.2d at 47.

<sup>83</sup> See *supra* note 67.

<sup>84</sup> Numerous jurisdictions hold that an existing violation of a zoning law constitutes an encumbrance. See *Wilcox*, 254 S.E.2d at 216 (minimum side lot violation); *Venisek*, 150 N.W.2d at 350 (minimum frontage requirement); *Lohmeyer*, 227 P.2d at 108 (minimum side lot violation); *Hebb v. Severson*, 201 P.2d 156, 158-59 (Wash. 1948) (violation of set-back

violations that neither constitute encumbrances within the covenant nor breach the guarantee to convey marketable title.

### **III. VIOLATIONS EXEMPTED FROM THE COVENANT AGAINST ENCUMBRANCES AND MARKETABLE TITLE**

Many courts have ruled out certain exceptions and found that because some violations do not affect title, they are not encompassed within the covenant against encumbrances. When a violation does not affect title, then the purchaser does not have a claim under the covenant and marketable title theories. The exceptions encompass a wide range of violations, although the rationale behind the exceptions is usually based upon the inherent difficulty in discovering the violation. There are some conflicting views within the jurisdictions regarding whether exceptions should be created based upon certain types of violations. The first exception deals with violations of building codes, which will be discussed in section A.<sup>85</sup> Another exception, although there is conflicting authority, deals with latent violations, which will be evaluated in section B.<sup>86</sup>

#### **A. Violations of Building Codes**

The first of these exceptions to the covenant against encumbrances and marketable title deals with building codes or similar regulations. The Supreme Court of Alaska, in *Domer v. Sleeper*,<sup>87</sup> held that where a building code violation is “unknown” or

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lines); *Moyer*, 164 A. at 111 (set-back requirement).

<sup>85</sup> See *infra* Part III.A.

<sup>86</sup> See *infra* Part III.B.

<sup>87</sup> 533 P.2d 9 (Alaska 1975).

“hidden,” then such a violation does not constitute an encumbrance.<sup>88</sup> In *Domer*, a building suffered considerable fire damage and a subsequent inspection revealed violations of a building code and fire code.<sup>89</sup> The Alaska court relied on a case from Washington that did not include the non-conforming condition of a building’s electrical wiring as an encumbrance.<sup>90</sup> The court explained that “[t]he state electrical inspector, may, under certain conditions, disconnect or order the discontinuance of electrical service, but that, while it may be an inconvenience and a restriction upon the use of the property, is not an encumbrance.”<sup>91</sup> Furthermore, “[w]hile electric, plumbing, sanitary, fire, safety, and building inspectors, and perhaps others, may restrict or prohibit the use of property in the exercise of the police power, . . . [this does not] constitute a breach of a covenant against encumbrances . . . .”<sup>92</sup> In holding that the violation of the building code is not encompassed within the covenant, the court stated that to hold otherwise would impose a substantial burden on a purchaser since violations are difficult to discover after construction has been completed.<sup>93</sup>

In *Fahmie v. Wulster*,<sup>94</sup> the New Jersey Supreme Court held that an existing pipe in a stream did not constitute an encumbrance.<sup>95</sup> The plaintiffs purchased an auto parts business by warranty deed that

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<sup>88</sup> *Id.* at 12.

<sup>89</sup> *Id.* at 10.

<sup>90</sup> *Id.* at 11-12.

<sup>91</sup> *Id.* at 12 (quoting *Stone v. Sexsmith*, 184 P.2d 567, 569 (Wash. 1947)).

<sup>92</sup> *Domer*, 533 P.2d at 12 (quoting *Stone*, 184 P.2d at 569).

<sup>93</sup> *Id.* at 13.

<sup>94</sup> 408 A.2d 789 (N.J. 1979).

<sup>95</sup> *Id.* at 790, 792.

included the covenant against encumbrances.<sup>96</sup> Subsequently, the plaintiffs wanted to sell to a corporation and both of the parties filed an application for a stream encroachment to construct a wall near a brook.<sup>97</sup> It was at this time that the plaintiffs learned that there was an existing pipe in the stream that was inadequate because of the size of the culvert.<sup>98</sup> The plaintiffs filed an action against the sellers to recover the expenses to install a new culvert so they could sell the property.<sup>99</sup> The court held that this did not constitute an encumbrance.<sup>100</sup>

The Supreme Court of New Jersey stated that “[t]o expand the concept of encumbrances . . . would create uncertainty and confusion in the law of conveyancing and title insurance. A title search would not have disclosed the violation, nor would a physical examination of the premises.”<sup>101</sup> The building violation did not constitute an encumbrance because a breach of the covenant against encumbrances is shown “ ‘when the proofs establish that a third person has a right to or an interest in the land conveyed, to the diminution of the value of the land, though consistent with the passing of the fee by the deed of conveyance.’ ”<sup>102</sup> This definition of encumbrance is narrow and it enabled the *Fahmie* court to hold that the building violation did not

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<sup>96</sup> *Id.* at 790.

<sup>97</sup> *Id.*

<sup>98</sup> *Id.* The previous seller had filed for an application to place a nine-foot culvert in the brook. The Bureau of Water Control responded by saying that this was not large enough “and that a 16’ X 5.5’ culvert” was necessary. This was ignored and the nine-foot culvert was installed. Subsequently, the sellers conveyed the property to plaintiffs. *Id.*

<sup>99</sup> *Id.*

<sup>100</sup> *Fahmie*, 408 A.2d at 792.

<sup>101</sup> *Id.*

<sup>102</sup> *Id.* at 791 (quoting *Gaier v. Berkow*, 217 A.2d 642 (N.J. Super. Ct. App. Div. 1966)).

create an encumbrance because by the limited definition, an encumbrance only exists when there is an interest by a third party.<sup>103</sup>

Other jurisdictions employ this same rationale. For instance, in *Domer* the court pointed to the Supreme Court of Washington that “defined encumbrance ‘to be any right to, or interest in, land which may subsist in third persons, to the diminution of the value of the estate of the tenant . . . .’ ”<sup>104</sup> Similarly, Maryland also restricts the covenant against encumbrances to protect “the covenantee . . . against rights or interests in the property conveyed which *subsist in third persons* and diminish the value of *the estate* . . . .”<sup>105</sup> When courts define an “encumbrance” narrowly, violations of building codes do not create an encumbrance because there is not necessarily an interested third party. This is perhaps one way courts have been able to exclude building code violations as encumbrances.

The majority of jurisdictions have similarly held that violations of building codes do not constitute encumbrances.<sup>106</sup> Another reason underlying this rule is that if the violations constituted encumbrances, this would “create instability in real estate transactions since every minor building and zoning code violation

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<sup>103</sup> See *supra* note 4. This definition of encumbrance is limiting when it applies to violations of ordinances.

<sup>104</sup> *Domer*, 533 P.2d at 11 (citing *Hebb v. Severson*, 201 P.2d 156, 160 (1948)).

<sup>105</sup> *Marathon Builders, Inc. v. Polinger*, 283 A.2d 617, 621 (Md. 1971).

<sup>106</sup> See *McRae v. Giteles*, 253 So. 2d 260, 261 (Fla. Dist. Ct. App. 1971) (“[T]he condition of the premises constituting the housing code violation is not an ‘encumbrance’ within the meaning of a warranty against encumbrances.”); *Abelman v. Slader*, 224 N.E.2d 569, 571 (Ill. 1967) (“[T]he existence of a building code violation does not of itself constitute a cloud on title . . . .”); *Sterbcow v. Peres*, 64 So. 2d 195, 201 (La. 1953) (“With reference to the failure to obtain a building permit, as required by the city ordinances, that of itself does not constitute a latent defect . . . .”); see also *Silverblatt v. Livadas*, 164 N.E.2d 875 (Mass. 1960); *Gaier v. Berkow*, 217 A.2d 642 (N.J. Super. 1966); *Gnash v. Saari*, 267 P.2d 674 (Wash. 1954).

would potentially cloud title.”<sup>107</sup> Due to the many violations of building codes, it is impractical to treat each violation as an encumbrance affecting title. This is certainly displayed in *McRae v. Giteles*<sup>108</sup> where even after the county’s housing department had found over eighty violations, a Florida court held that the violations did not constitute an encumbrance.<sup>109</sup>

Notably, a few states, including Wisconsin and North Carolina, have moved away from such a rigid application of this rule. In *Brunke v. Pharo*,<sup>110</sup> an apartment building was conveyed to buyers, who upon purchasing, the Supreme Court of Wisconsin said were “violators of the law,” because there was a violation of a building code.<sup>111</sup> Before the property had even been conveyed, a commission issued a certificate compelling the sellers to take action and remedy the building code violation.<sup>112</sup> The court held that where an agency has compelled enforcement requiring action to be taken to remedy the violation, this constitutes an encumbrance.<sup>113</sup> Thus, the limited holding applies to situations where a governmental agency requires a party to fix the building in order to comply with the code or regulation. While injured buyers have tried to rely on *Brunke* in seeking relief, many times no enforcement has taken place yet and

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<sup>107</sup> FFG, Inc. v. Jones, 708 P.2d 836, 846 (Haw. Ct. App. 1985).

<sup>108</sup> *McRae*, 253 So. 2d 260.

<sup>109</sup> *Id.* at 260, 262.

<sup>110</sup> 89 N.W.2d 221 (Wis. 1958).

<sup>111</sup> *Id.* at 222.

<sup>112</sup> *Id.*

<sup>113</sup> *Id.* at 223 (“[A] violation of this type of regulation with respect to which the agency charged with enforcement has begun to take official action is an incumbrance [sic].”).

therefore *Brunke* is distinguishable.<sup>114</sup> Also, in *Brunke*, the violations were noticed prior to conveyance,<sup>115</sup> which is also a distinguishing factor pointed out in *FFG, Inc. v. Jones*<sup>116</sup> and *Fahmie*.<sup>117</sup>

In addition to the Supreme Court of Wisconsin, the North Carolina Court of Appeals, in *First American Federal Savings & Loan Association v. Royall*,<sup>118</sup> held that a violation of a building code constitutes an encumbrance.<sup>119</sup> A developer violated a municipal code that required developers to connect a water system between lots when constructing a subdivision.<sup>120</sup> The court held this breach to be a violation of the covenant against encumbrances.<sup>121</sup> This is distinguishable from most building code cases that do not find an encumbrance because the failure to connect a water system is by no means “unknown” or “hidden.”<sup>122</sup>

Taken as a whole, most jurisdictions have held that a violation of a building code or similar regulation does not constitute an encumbrance.<sup>123</sup> Therefore, under the majority rule, when a purchaser discovers a violation, and is perhaps subject to penalties, fines or must take remedial action in order to comply, which may be

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<sup>114</sup> See, e.g., *Gaier*, 217 A.2d at 643 (“Nor are we confronted here with a situation where prosecution was imminent when the deed was executed.”).

<sup>115</sup> *Brunke*, 89 N.W.2d at 222 (“[P]rior to the conveyance, a representative of the commission had inspected the premises and the commission had determined, administratively, that the violations existed.”).

<sup>116</sup> *FFG, Inc.*, 708 P.2d at 846.

<sup>117</sup> 408 A.2d 789, 792.

<sup>118</sup> 334 S.E.2d 792 (N.C. Ct. App. 1985).

<sup>119</sup> *Id.* at 796.

<sup>120</sup> *Id.* at 795.

<sup>121</sup> *Id.* at 796.

<sup>122</sup> See *supra* note 88 and accompanying text.

<sup>123</sup> See *supra* note 106.

expensive, the purchaser is left with no remedy against the seller, even when the seller knew of the violation. This may be devastating to a consumer that just bought a piece of property unaware of existing violations. One way to limit this exposure would be for a buyer to hire a licensed engineer to inspect the property prior to signing a contract.

### **B. Latent Defects Do Not Constitute Encumbrances**

Another similar exception to the general rule was set forth in *Frimberger v. Anzellotti*.<sup>124</sup> The court held that encumbrances “cannot be expanded to include *latent conditions* on property that are in violation of statutes or governmental regulations.”<sup>125</sup> The concept of “hidden” or “latent” violations expands beyond building code violations, as is evident in the following cases.

#### **1. *Frimberger v. Anzellotti***

*Frimberger* involved a tidal wetlands violation (as opposed to a building code violation).<sup>126</sup> A predecessor in title subdivided a piece of land for the purpose of constructing residences.<sup>127</sup> Because the property was adjacent to a tidal marshland, it was subject to statutory provisions, which dealt with wetland protection.<sup>128</sup> The predecessor, DiLoreto, built a bulkhead near the wetlands and

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<sup>124</sup> 594 A.2d 1029 (Conn. App. Ct. 1991). *Frimberger*, notably was decided the same year the Georgia court decided *Barnett*.

<sup>125</sup> *Id.* at 1034 (emphasis added).

<sup>126</sup> By contrast, this is different from a municipal zoning ordinance.

<sup>127</sup> *Frimberger*, 594 A.2d at 1031.

<sup>128</sup> *Id.* (concerning the preservation of tidal wetlands due to the loss of much of the wetlands in Connecticut).

constructed a dwelling.<sup>129</sup> He transferred the property to the defendant,<sup>130</sup> who then conveyed the property to the plaintiff by warranty deed “free and clear of all encumbrances but subject to all building, building line and zoning restrictions as well as easements and restrictions of record.”<sup>131</sup> The plaintiff wanted to make repairs on the bulkhead so the State Department of Environmental Protection (“DEP”) took a survey of the property.<sup>132</sup> The DEP informed the plaintiff that there was a tidal wetlands violation and that the filled bulkhead part of the property, together with the northwest corner of the house, constituted an encroachment on the tidal wetlands.<sup>133</sup> In order to correct this, the plaintiff was told by the DEP that he could submit an application demonstrating the necessity for the bulkhead and portion that went within the tidal wetlands.<sup>134</sup> Alternatively, the plaintiff decided to sue the defendant for breach of warranty against encumbrances and innocent misrepresentation.<sup>135</sup>

In reaching its decision, the court relied on other decisions that have held that building code violations do not constitute encumbrances.<sup>136</sup> The court explained that there was authority “to support the proposition that such an exercise of police power by the state *does not* affect the marketability of title and should not rise to

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<sup>129</sup> *Id.*

<sup>130</sup> This transfer was by a quitclaim deed. *Id.*

<sup>131</sup> *Id.*

<sup>132</sup> *Frimberger*, 594 A.2d at 1031.

<sup>133</sup> *Id.*

<sup>134</sup> *Id.*

<sup>135</sup> *Id.*

<sup>136</sup> These include the cases discussed previously. *See supra* notes 87-123 and accompanying text.

the level of an encumbrance.”<sup>137</sup> Relying on *Fahmie*, the *Frimberger* court stated that an “enlargement of the covenant against encumbrances would create uncertainty and confusion in the law of conveyancing and title insurance because neither a title search nor a physical examination of the premises would disclose the violation.”<sup>138</sup> Hence, this case is similar to *Fahmie* because the violation was “not on the land records and was discovered only after the plaintiff attempted to get permission to perform additional improvements to the wetlands area.”<sup>139</sup> Therefore, when latent violations occur that do not show up on land records, the violation does not constitute an encumbrance.<sup>140</sup>

Perhaps if the DEP had not requested the plaintiff to make an application to show the necessity of the bulkhead, but had compelled compliance with the statute, the result would have been different. The court focuses on the fact that “there had been no further action taken by the DEP to compel compliance, and no administrative order was ever entered from which the plaintiff could appeal.”<sup>141</sup> If action were taken to compel compliance, the result would have perhaps

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<sup>137</sup> *Frimberger*, 594 A.2d at 1032. See *supra* notes 94-103 and accompanying text.

<sup>138</sup> *Frimberger*, 594 A.2d at 1033.

<sup>139</sup> *Id.*

<sup>140</sup> The court uses the following language to define its holding:

Latent violations of state or municipal land use regulations that do not appear on the land records, that are unknown to the seller of the property, as to which the agency charged with enforcement has taken no official action to compel compliance at the time the deed was executed, and that have not ripened into an interest that can be recorded on the land records do not constitute an encumbrance for the purpose of the deed warranty.

*Id.* at 1033-34.

<sup>141</sup> *Id.* at 1033.

been the opposite. This would have most likely been the case if the *Brunke* decision from Wisconsin was followed.<sup>142</sup> An important aspect of the *Frimberger* case is that the plaintiff was not ordered to comply with the statute as of the date of trial, which may have affected the outcome. Therefore, the concern of undue burden on the buyer was not present in *Frimberger*.

## 2. *Bianchi v. Lorenz*

In 1997, the Supreme Court of Vermont decided *Bianchi v. Lorenz*,<sup>143</sup> where the court had to confront the *Frimberger* case. The sellers wanted to install a septic system for a four-bedroom home; however, the technician they hired discovered that because of the small size of the lot, it would not be feasible to install a septic system large enough for a four-bedroom home.<sup>144</sup> The sellers obtained a building permit and it provided “that all construction [was] to be completed in accordance with the Zoning Laws of the Town of Jericho and State of Vermont.”<sup>145</sup> Jericho’s zoning ordinance required an owner to apply for a certificate of occupancy after constructing a new home and the certificate would only be issued if the home is found to be in compliance with building and septic permits.<sup>146</sup> The zoning ordinance provided that a building could not be occupied until the certificate of occupancy was issued.<sup>147</sup>

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<sup>142</sup> See *supra* note 110.

<sup>143</sup> 701 A.2d 1037 (Vt. 1997).

<sup>144</sup> *Id.* at 1038.

<sup>145</sup> *Id.* (quotations omitted).

<sup>146</sup> *Id.*

<sup>147</sup> *Id.*

Furthermore, the permit that the sellers obtained said that “the septic tank was ‘to be constructed in accordance with [the] design by [the site technician].’ ”<sup>148</sup>

The sellers did not adhere to the technician’s findings and the town did not issue a certificate of occupancy.<sup>149</sup> Subsequently, the sellers sold to the buyers, not giving them any notification of the defective septic system.<sup>150</sup> Several months later, the buyers noticed that the portion of grass near the septic tank was “unusually lush,” which led to surfacing “septic effluent.”<sup>151</sup> It was at this time that an engineer told them that the septic tank was not in accordance with the technician’s plans.<sup>152</sup> A town health officer informed them that they must obtain a certificate of occupancy to comply with zoning laws and in order to do so, they must replace the septic system.<sup>153</sup>

The buyers sued the sellers to recover the costs to repair the septic system; relief was granted.<sup>154</sup> The sellers argued that a violation of a zoning ordinance is latent and not discoverable, relying on *Frimberger*.<sup>155</sup> The sellers maintained that the violation could not be found in land records.<sup>156</sup> The court relied on *Hunter Broadcasting, Inc. v. City of Burlington*,<sup>157</sup> decided two years prior,

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<sup>148</sup> *Bianchi*, 701 A.2d at 1038 (quotations omitted).

<sup>149</sup> *Id.*

<sup>150</sup> *Id.* Sellers conveyed by a general warranty deed including the covenant against encumbrances. *Id.*

<sup>151</sup> *Id.*

<sup>152</sup> *Id.* at 1038-39.

<sup>153</sup> *Bianchi*, 701 A.2d at 1038-39.

<sup>154</sup> *Id.* at 1039.

<sup>155</sup> *Id.* at 1040.

<sup>156</sup> *Id.*

<sup>157</sup> 670 A.2d 836 (Vt. 1995). In this case, a seller conveyed a parcel that had not received state subdivision approval. A statute required a subdivision approval permit for the resale of

which held that a violation of a public health regulation that required a subdivision permit was an encumbrance for purposes of the covenant against encumbrances.<sup>158</sup> The court employed *Hunter Broadcasting* by stating “a violation is not latent merely because the purchaser examines the records of a separate agency.”<sup>159</sup> The *Bianchi* court took the position that it does not matter what type of public records a buyer must search in the determination of whether a certain violation is an encumbrance for purposes of the covenant against encumbrances.<sup>160</sup>

Furthermore, the court focused on the fact that it is the seller’s duty to determine whether a certificate of occupancy has been issued to comply with the zoning ordinance. The court explained that “[i]f no certificate has been issued, the owner must bring the property into zoning compliance by meeting zoning permit requirements for an occupancy permit.”<sup>161</sup> In effect, the court adopted the position that sellers have the duty to determine from municipal records whether there is an encumbrance and take the necessary measures so their property will comply with ordinances.<sup>162</sup>

To summarize, where there is a latent violation of a zoning ordinance, the covenant against encumbrances is not breached. Yet, the *Bianchi* court did not accept the proposition that the violation was

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certain property. The purchaser sued under the covenant against encumbrances. The court found that the failure to obtain subdivision approval was an encumbrance that affected title. *Id.* at 837-89.

<sup>158</sup> *Bianchi*, 701 A.2d at 1039 (citing *Hunter Broadcasting, Inc.*, 670 A.2d at 839).

<sup>159</sup> *Id.* at 1040.

<sup>160</sup> *Id.* at 1040-41.

<sup>161</sup> *Id.* at 1041.

<sup>162</sup> *Id.* “The theory which we have adopted allows subsequent sellers and buyers to determine whether there is an encumbrance from municipal records.” *Id.*

latent, even though the violation could not be found in public records. The court went beyond rejecting the argument that the violation was not an encumbrance, and discussed the seller's duty to make sure that existing land uses are in compliance with restrictions. *Bianchi* could be placed into the same category as those cases that have held that a violation of a zoning ordinance constitutes an encumbrance. However, when viewed in light of *Frimberger*, it appears to contrast *Frimberger's* departure when the violation is latent. In *Bianchi*, the violation appeared to be latent, but instead of focusing on its being latent, the court discussed the need to ensure compliance with municipal ordinances. The *Frimberger* and *Bianchi* cases represent the two theories in the area of latent violations. However, *Frimberger* can also be viewed as being treated differently because it was a state governmental regulation, rather than a zoning ordinance. How far the concept of latent violations will be extended is a question that will be answered as more courts in the future confront the *Frimberger* decision.

Numerous violations of zoning ordinances and land use restrictions have been at issue in every state. There are widespread violations of ordinances, some of them going unnoticed for lengthy periods of time.<sup>163</sup> Many violations are difficult to discover, as illustrated in the case law concerning building code violations and latent violations. Because of the inherent difficulty in discovering violations and because it is not required or customary for sellers to

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<sup>163</sup> Freyfogle, *supra* note 14, at 1 ("With enforcement so inconsistent, land use violations can for years remain uncorrected and even undetected.").

discover violations, some courts have narrowed the scope of the covenant against encumbrances and marketable title claims. Limiting the scope of these avenues for relief cultivates noncompliance with ordinances and regulations. The *Bianchi* court stated that it is a seller's duty to make sure that existing land uses are in compliance with restrictions. If *Bianchi* were followed, which requires more of sellers, it would also follow that sellers have a duty to keep their property in compliance with ordinances and have a greater duty to disclose. Purchasers are disadvantaged without a remedy against the seller, and there is a higher probability that sellers will not comply with zoning ordinances if courts continue to hold that certain violations are not encompassed within the scope of marketable title guarantee or the covenant against encumbrances. These exceptions are problematic, especially in light of the permissive duty on sellers to disclose violations.

#### **IV. DUTIES ON BUYERS AND SELLERS: LOOKING FOR RELIEF WHEN A SELLER DOES NOT HAVE TO DISCLOSE A VIOLATION**

Part IV illustrates the problems that purchasers face in discovering violations of zoning ordinances and regulations, and in addition, how other potential avenues for relief will likely fail, which leaves purchasers unprotected. First, Part IV explores the duties that sellers have in relation to disclosing zoning ordinance violations, which includes a discussion relating to the caveat emptor doctrine in section A.<sup>164</sup> Section B explores the departure from the caveat

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<sup>164</sup> See *infra* Part IV.A.

emptor rule among the jurisdictions through either case law or via the legislature.<sup>165</sup> Section B will include a discussion of some of the legislation that has been enacted concerning the duty to disclose on sellers, including property disclosure statutes. Second, Part IV discusses how other potential remedies for a plaintiff, such as recovery in tort under a theory of misrepresentation or a claim against a title insurance company, is insufficient to protect a purchaser when there is an existing zoning violation. Section C will evaluate the insufficiencies of these remedies.<sup>166</sup>

#### **A.      Caveat Emptor Rule**

The duty on buyers to inspect the land is known as the caveat emptor doctrine. The caveat emptor or “buyer beware” rule says that in the absence of an agreement, a seller has no duty to inform the buyers of defects in the condition of the property.<sup>167</sup> The doctrine “was derived from the political philosophy of laissez-faire, which mandated that a buyer deserved whatever he got if he relied on his own inspection of the merchandise and did not extract an express warranty from the seller.”<sup>168</sup> The rule evolved in land transactions where “both the buyer and seller were generally farmers with similar levels of bargaining power and the availability of the seller’s defense

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<sup>165</sup> See *infra* Part IV.B.

<sup>166</sup> See *infra* Part IV.C.

<sup>167</sup> Robert H. Shisler, Note, *Caveat Emptor is Alive and Well and Living in New Jersey: A New Disclosure Statute Inadequately Protects Residential Buyers*, 8 FORDHAM ENVTL. L.J. 181, 184 (1996) (discussing the beginnings of the caveat emptor rule).

<sup>168</sup> Florrie Y. Roberts, *Disclosure Duties in Real Estate Sales and Attempts to Reallocate the Risk*, 34 CONN. L. REV. 1, 4 (2001) (quotations omitted). Roberts argues that sellers and buyers should be able to contract around the seller’s duty to disclose; that it would be economically efficient, it would promote certainty, avoid litigation, and would promote

of caveat emptor created a heavy incentive for the buyer to fully inspect the property because representations and obligations made to the buyer integrated with the deed upon delivery.”<sup>169</sup> Buyers, upon discovering latent defects, could only seek legal recourse if they had protected themselves with express warranties.<sup>170</sup>

### B. Departures From the Caveat Emptor Rule

A departure from the caveat emptor rule began in the middle of the twentieth century.<sup>171</sup> When developers began to “build dozens of homes at one time,” this evolved into the more modern real estate marketplace.<sup>172</sup> As a result, “since the builder/seller is the one who actually built the homes, superior knowledge about the structure, property, and surrounding areas is obviously conferred.”<sup>173</sup> Because the seller then has more knowledge about the property, courts moved to protect the buyer by creating a duty to disclose material latent defects and an implied warranty of habitability.<sup>174</sup> The implied warranty of habitability was created in the courts at or about the time the courts were abandoning the caveat emptor rule. In 1964, the Supreme Court of Colorado was the first court to abandon the doctrine of caveat emptor, when it held that a builder of a home impliedly warrants that it complies with applicable building code requirements, is built in a workmanlike manner, and is suitable for

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marketability of property. *Id.* at 2-3.

<sup>169</sup> Shisler, *supra* note 167, at 184 (footnotes omitted).

<sup>170</sup> *Id.* at 185.

<sup>171</sup> Roberts, *supra* note 168, at 5.

<sup>172</sup> Shisler, *supra* note 167, at 185.

<sup>173</sup> *Id.*

<sup>174</sup> *Id.* at 185-86.

habitation.<sup>175</sup>

Many jurisdictions have rejected or narrowed the doctrine of caveat emptor.<sup>176</sup> The Supreme Court of Alaska, in 1980, discussed the split of authority regarding a buyer's duty and noted that the trend "is toward placing a minimal duty on a buyer."<sup>177</sup> The court explained that "[a] person guilty of fraudulent misrepresentation should not be permitted to hide behind the doctrine of *caveat emptor*."<sup>178</sup> The court held that "a defense based upon lack of due care should not be allowed in land sales contracts where a reckless or knowing misrepresentation has been made."<sup>179</sup> Since 1980, the courts and legislatures have followed this reasoning and have further curtailed the doctrine of caveat emptor. California is a forerunner by creating a broad duty on sellers to disclose defects.<sup>180</sup> Most states use a standard of materiality in defining what defects need to be disclosed; a seller need not disclose every minor defect.<sup>181</sup> The courts have primarily used an objective approach, in which a seller does not need to disclose minor defects that would not concern

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<sup>175</sup> *Carpenter v. Donohoe*, 388 P.2d 399, 402 (Colo. 1964).

<sup>176</sup> *Roberts*, *supra* note 168, at 5 ("Within the last forty years . . . the law has taken a sharp turn. Courts and legislatures have imposed ever increasing duties on sellers to disclose to prospective buyers information about the property being sold.").

<sup>177</sup> *Cousineau v. Walker*, 613 P.2d 608, 614 (Alaska 1980).

<sup>178</sup> *Id.* (citing *Upledger v. Vilanor*, 369 So.2d 427, 430 (Fla. Dist. Ct. App. 1979)).

<sup>179</sup> *Id.* (citation omitted). For cases supporting this proposition see, for example, *Piazzini v. Jessup*, 314 P.2d 196, 198 (Cal. Ct. App. 1957); *Sorenson v. Adams*, 571 P.2d 769, 776 (Idaho 1977); *Fox v. Wilson*, 507 P.2d 252, 266 (Kan. 1973); *Kannavos v. Annino*, 247 N.E.2d 708, 712 (Mass. 1969); *Heverly v. Kirkendall*, 478 P.2d 381, 383 (Or. 1970).

<sup>180</sup> *Roberts*, *supra* note 168, at 5-6 (stating that in California, when a seller "knows of facts materially affecting the value" and within the "reach of the diligent attention" of the buyer, the seller has the duty to disclose (citing *Shapiro v. Sutherland*, 76 Cal. Rptr. 2d 101, 107 (Cal. Ct. App. 1998))).

<sup>181</sup> *Id.* at 10.

“ordinary sellers and buyers.”<sup>182</sup>

In addition to courts overturning caveat emptor, legislatures have attempted to protect buyers by enacting property disclosures statutes.<sup>183</sup> Approximately thirty-six states have property disclosure legislation.<sup>184</sup> While some states have enacted property disclosure statutes and rejected the doctrine of caveat emptor, some jurisdictions have retained the rule.<sup>185</sup> Massachusetts,<sup>186</sup> Indiana,<sup>187</sup> Alabama,<sup>188</sup> and Minnesota<sup>189</sup> fall within this category. New York has a property disclosure statute, but has fallen short of protecting purchasers. In 1991, in *Stambovsky v. Ackley*,<sup>190</sup> the court stated “New York law fails to recognize any remedy for damages incurred as a result of the seller’s mere silence, applying instead the strict rule of caveat emptor.”<sup>191</sup> Then, in 2002, the New York legislature enacted the New York Property Condition Disclosure Act.<sup>192</sup> A seller may

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<sup>182</sup> *Id.*

<sup>183</sup> The property disclosure statutes, each varying from one another, require the seller to make certain disclosures about the condition of the property. *See, e.g.*, IDAHO CODE ANN. § 55-2508 (2006) (including numerous questions to be filled out by the seller, which includes conditions that might affect the clearance of title); 765 ILL. COMP. STAT. ANN. 77/35 (LexisNexis 2006) (including questions regarding what the seller has actual knowledge of).

<sup>184</sup> Philip Lucrezia, Recent Development, *New York’s Property Condition Disclosure Act: Extensive Loopholes Leave Buyers and Sellers of Residential Real Property Governed by the Common Law*, 77 ST. JOHN’S L. REV. 401, 417 (2003).

<sup>185</sup> Roberts, *supra* note 168, at 13-14. *See* Freyfogle, *supra* note 14, at 1-2 (“The caveat emptor doctrine, despite recent criticism, remains the rule governing unlawful land usages: the buyer has the responsibility for determining whether existing land uses are unlawful by inspecting the property, reviewing municipal ordinances, and checking the seller’s title.”).

<sup>186</sup> *See* Solomon v. Birger, 477 N.E.2d 137, 142 (Mass. App. Ct. 1985).

<sup>187</sup> *See* Indiana Bank & Trust Co. v. Perry, 467 N.E.2d 428, 431 (Ind. Ct. App. 1985).

<sup>188</sup> *See* Blaylock v. Cary, 709 So. 2d 1128, 1130 (Ala. 1997).

<sup>189</sup> *See* Klein v. First Edina Nat’l Bank, 196 N.W.2d 619, 622 (Minn. 1972) (finding a duty to disclose in three situations, which are very narrow).

<sup>190</sup> 572 N.Y.S.2d 672 (App. Div. 1991).

<sup>191</sup> *Id.* at 675.

<sup>192</sup> N.Y. REAL PROP. LAW §§ 460-67 (McKinney 2006). Section 462 states in pertinent part: “[E]very seller of residential real property pursuant to a real estate purchase contract

choose to pay a \$500 credit to the purchaser and not be required to make any disclosures.<sup>193</sup> Consequently, “[t]he apparent consensus is that attorneys representing sellers are counseling their clients to simply provide the \$500 credit to buyers rather than subject themselves to possible liability in the future.”<sup>194</sup> Connecticut and Rhode Island also have property disclosure statutes that allow sellers to pay money to remove them from the scope of the act.<sup>195</sup> Providing an option for sellers to simply rid themselves of any disclosure by paying a sum of money leaves buyers with the common law caveat emptor rule. The real estate market tends to suggest that prospective purchasers are “ready to make offers and waive their rights.”<sup>196</sup>

Furthermore, some jurisdictions provide a means to allocate the risks of disclosure. These jurisdictions allow a seller to disclaim liability, usually by giving the seller the option of either providing a disclosure statement or a disclaimer form containing an “as is”

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shall complete and sign a property condition disclosure statement . . . to be delivered to a buyer or buyer’s agent prior to the signing by the buyer of a binding contract of sale.” Moreover, Section 465 provides that:

In the event a seller fails to perform the duty prescribed in this article to deliver a disclosure statement prior to the signing by the buyer of a binding contract of sale, the buyer shall receive upon the transfer of title a credit of five hundred dollars against the agreed upon purchase price of the residential real property.

<sup>193</sup> *Id.*

<sup>194</sup> Lucrezia, *supra* note 184, at 411-12.

<sup>195</sup> *Id.* at 414; *see also* CONN. GEN. STAT. ANN. § 20-327c (West 2006) (“On or after January 1, 1996, every agreement to purchase residential real estate . . . shall include a requirement that the seller credit the purchaser with the sum of three hundred dollars at closing should the seller fail to furnish the written residential condition report as required by sections 20-327b to 20-327e, inclusive.”); R.I. GEN. LAWS § 5-20.8-5(b) (2006) (“Failure to provide the seller disclosure form to the buyer does not void the agreement nor create any defect in title. Each violation of this statute by the seller and/or his or her agent is subject to a civil penalty in the amount of one hundred dollars (\$ 100) per occurrence.”).

<sup>196</sup> Lucrezia, *supra* note 184, at 421.

clause.<sup>197</sup> Tennessee,<sup>198</sup> Maryland,<sup>199</sup> and North Carolina<sup>200</sup> are among the states that have such statutes.<sup>201</sup> These property disclosure statutes insufficiently protect buyers because the sellers are given full discretion whether they choose to disclose anything to the purchasers. Again, when the property disclosure statutes have loopholes and gaps, the purchaser is left unprotected and must rely on the common law, many times at the mercy of the caveat emptor rule.<sup>202</sup> Moreover, property disclosure statutes typically do not require disclosure of violations of zoning ordinances.

### C. Potential Relief under a Theory of Misrepresentation or against a Title Insurance Company?

If, in many jurisdictions, a purchaser is at the mercy of the caveat emptor rule, he or she may look to other potential avenues for

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<sup>197</sup> Roberts, *supra* note 168, at 20; *see also* VA. CODE ANN. § 55-519 (2006).

<sup>198</sup> TENN. CODE ANN. § 66-5-202(2) (2006) states:

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 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 disclaimer statement may only be permitted where the purchaser waives the required disclosure under subdivision (1). If the purchaser does not waive the required disclosure under this part, the disclosure statement described in subdivision (1) shall be provided in accordance with the requirements of this part.

<sup>199</sup> MD. CODE ANN., REAL PROP. § 10-702(d) (LexisNexis 2006) (setting forth an extensive disclaimer).

<sup>200</sup> N.C. GEN. STAT. § 47E-4(a)(2) (2006) ("The disclosure statement shall: . . . State that the owner makes no representations as to the characteristics and condition of the real property or any improvements to the real property except as otherwise provided in the real estate contract.").

<sup>201</sup> Roberts, *supra* note 168, at 20. *See also* 765 ILL. COMP. STAT. ANN. 77/35 (LexisNexis 2007).

<sup>202</sup> Moreover, the case law suggests that "there is no duty to disclose zoning ordinance violations, unless provided for in some way between the parties." Forman, *supra* note 3, at

2007]      *MARKETABLE TITLE AND ENCUMBRANCES*      233

relief. One possible avenue is under a tort theory of misrepresentation. Also, perhaps a purchaser can look for relief from the title insurance company that issued the title report to the purchaser which included provisions concerning any existing encumbrances.

As for tort misrepresentation recovery, this potential relief may not benefit the buyer. Buyers suffer additional risks because it is often difficult for a plaintiff to recover under a misrepresentation theory because of the inability to prove the existence of a false statement of fact.<sup>203</sup> For example:

[A]ssertions about the zoning status of property, the permissibility of some existing or proposed use under a zoning ordinance, a building's compliance with building codes, the consistency of some specified use with a local development standard, and the need to obtain a permit before engaging in a particular activity have all been viewed by courts as opinions of law that cannot give rise to tort liability.<sup>204</sup>

Although courts have expanded misrepresentation law by treating more of sellers' statements as being actionable, it is still difficult for purchasers to recover under tort misrepresentation law.<sup>205</sup> It is hard for a buyer to prove that he actually relied on the seller's

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<sup>203</sup> Freyfogle, *supra* note 14, at 6.

<sup>204</sup> *Id.* (citing *Davis v. Northside Realty*, 299 S.E.2d 186 (Ga. Ct. App. 1983); *City of Aurora v. Green*, 467 N.E.2d 610 (Ill. App. Ct. 1984); *O'Brien v. Noble*, 435 N.E.2d 554 (Ill. App. Ct. 1982); *Scott v. Wilson*, 146 N.E.2d 297 (Ill. App. Ct. 1958); *Northernaire Prods v. County of Crow Wing*, 244 N.W.2d 279 (Minn. 1976)).

<sup>205</sup> *Id.* at 7-8. For more information about expanding the scope of misrepresentation liability, see Freyfogle, *supra* note 14, at 8-17.

statement and that the seller possessed the requisite scienter.<sup>206</sup> One reason it is difficult to prove actual reliance is because buyers can “check a statement’s accuracy by reviewing zoning maps, searching deeds and encumbrances of record, or making inquiries of municipal code enforcers.”<sup>207</sup>

Therefore, violations are difficult to discover because a purchaser may need to search extensive public records containing zoning ordinances, municipal ordinances, and land use restrictions, to prove actual reliance.<sup>208</sup> Requiring searches imposes a considerable burden on buyers.<sup>209</sup> It is customary for buyers to contract with title insurance companies to locate any encumbrances on the title. Yet, often the buyer is still left unprotected because of the difficulties inherent in public records searches. Clearly, reform is needed in order to protect purchasers when a buyer cannot prove the requisite elements for misrepresentation, which will be discussed.<sup>210</sup>

Further discussion of the *Bianchi*<sup>211</sup> decision, in Vermont, provides an example and illustration of the potential complications jurisdictions are having with recording requirements. The *Bianchi* decision caused much confusion among title examiners and town clerks in Vermont because it was unclear exactly what type of public

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<sup>206</sup> *Id.*

<sup>207</sup> *Id.* at 13; *see, e.g.*, *Steinberg v. Bay Terrace Hotel, Inc.*, 375 So. 2d 1089, 1092 (Fla. Dist. Ct. App. 1979) (denying rescission for buyers when they could have inspected zoning and building records prior to closing); *Green*, 467 N.E.2d at 613 (denying misrepresentation claim because plaintiffs failed to make municipal inquiries); *NRC, Inc. v. Pickhardt*, 667 S.W.2d 292, 293-94 (Tex. App. 1984) (buyer has no right to rely on statement contrary to recorded title).

<sup>208</sup> *See supra* note 138 and accompanying text.

<sup>209</sup> Freyfogle, *supra* note 14, at 13.

<sup>210</sup> *See infra* Part V.

<sup>211</sup> *See supra* notes 143-164 and accompanying text.

records had to be searched.<sup>212</sup> The Vermont Supreme Court clearly established that a “title examiner or attorneys must examine not only traditionally-maintained town registries, but ill-kept town zoning and permitting records as well.”<sup>213</sup> Town clerks had to come up with a recording system that would provide permit records.<sup>214</sup> The problem here is an example of the different dilemmas various states may already have or will confront when an encumbrance constitutes a failure to obtain a permit that will in turn represent a violation of a municipal ordinance.

As a result, Vermont enacted a statute, explicitly overruling *Bianchi* that provided: “[n]o encumbrance on record title to real estate or effect on marketability shall be created by the failure to obtain or comply with the terms or conditions of any required municipal land use permit . . . .”<sup>215</sup> The law required town clerks to record permits and notices of permit violations, as well as notices of ordinance violations relating to land use.<sup>216</sup> Although these statutes

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<sup>212</sup> Jeremy I. Farkas, Feature, *Real Property Law - Bianchi II/S.144*, 25 VT. B. J. & L. DIG. 57, 57 (1999).

<sup>213</sup> *Id.*

<sup>214</sup> *Id.*

<sup>215</sup> VT. STAT. ANN. tit. 27, § 612 (2006).

<sup>216</sup> VT. STAT. ANN. tit. 24, § 1154 (2006) states in pertinent part:

(a) A town clerk shall record in the land records, at length or by accurate, legible copy, in books to be furnished by the town: . . . (6) municipal land use permits . . . or notices of municipal land use permits . . . notices of violation of ordinances or bylaws relating to municipal land use, and notices of violation of municipal land use permits; (7) denials of municipal land use permits. . . .

(b) A notice of a municipal land use permit or a notice of violation specified in subdivision (a)(6) of this section may be recorded, and if such notice is recorded, it shall list: (1) as grantor, the owner of record title to the property at the time the municipal land use permit or notice of violation is issued; (2) as grantee, the municipality issuing the permit, certificate or notice; (3) the municipal or village office where the

affected how the covenant against encumbrance and marketable title claims would be treated, it did not foreclose on the issue of the duties of title examiners. Title examiners still continue to search municipal permit records in order to meet their duties to their clients.<sup>217</sup> Purchasers may seek relief from the title insurance company when it breaches its duties.<sup>218</sup>

Seeking relief from a title insurance company was shown in *New England Federal Credit Union v. Stewart Title Guarantee Co.*,<sup>219</sup> another Vermont decision. Stewart Title issued a policy to purchasers that excluded land use regulations, but an exception to this included “a defect, lien or encumbrance resulting from a violation or alleged violation affecting the land [that] has been recorded in the public records.”<sup>220</sup> The purchasers wanted to sell the property, but upon discovering a violation of a failure to obtain a permit for a wastewater system erected twenty years prior, they were unable to sell.<sup>221</sup> New England Federal Credit Union (“NEFCU”) foreclosed on the property and issued a notice of claim to Stewart Title for the loss of value.<sup>222</sup> Upon denial, NEFCU sued.<sup>223</sup>

The Supreme Court of Vermont explained that the issue

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original, or a true, legible copy of the municipal land use permit may be examined; (4) whether an appeal of such permit, certificate, or notice has been taken; (5) tax map lot number or other description identifying the lot.

<sup>217</sup> Farkas, *supra* note 212, at 58.

<sup>218</sup> *Id.*

<sup>219</sup> 765 A.2d 450 (Vt. 2000).

<sup>220</sup> *Id.* at 452 (emphasis added).

<sup>221</sup> *Id.*

<sup>222</sup> *Id.*

<sup>223</sup> *Id.*

depended upon the meaning of encumbrance for purposes of the title insurance policy, as opposed to the covenant against encumbrances in the warranty deed.<sup>224</sup> It is therefore necessary, the court said, to look at the title policy and the intent of the parties.<sup>225</sup> The term “public records” stated within the policy encompassed the records that would reveal the subdivision permits or violations.<sup>226</sup> The court discussed in-depth what exactly “public records” includes.<sup>227</sup> It pointed to an Alaska decision that concluded that “public records” did not exclude an order filed with the office of a registrar in Washington, D.C.<sup>228</sup> and an Illinois decision that “public records” included records of the circuit court of the county.<sup>229</sup> The term “public records” therefore was not limited to municipal land records, but encompassed subdivision permit records of the Department of Environmental Conservation, a state agency that, pursuant to state law, imparted constructive notice of permits or violations.<sup>230</sup> This result was partly due to the fact that “ ‘Vermont’s subdivision regulations are sufficiently precise.’ ”<sup>231</sup> The Vermont case, as well as others, questioned the duties of title insurance companies in providing notice of violations of ordinances and regulations.

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<sup>224</sup> *Stewart*, 765 A.2d at 453. *Hunter Broadcasting* had to be distinguished in that it involved a lack of state subdivision approval that affected the warranty against encumbrances. *Id.*

<sup>225</sup> *Id.*

<sup>226</sup> *Id.* at 455.

<sup>227</sup> *Id.*

<sup>228</sup> *Id.* (citing *Hahn v. Alaska Title Guar. Co.*, 557 P.2d 143, 145-47 (Alaska 1976)).

<sup>229</sup> *Stewart*, 765 A.2d at 455 (citing *Radovanov v. Land Title Co. of Am.*, 545 N.E.2d 351, 355 (Ill. App. Ct. 1989)).

<sup>230</sup> *Id.* at 455.

<sup>231</sup> *Id.* at 454 (quoting *Hunter Broadcasting*, 670 A.2d at 840).

Numerous other cases, like *Stewart*, questioned title insurance companies' duty to provide notice of ordinance violations. In *1119 Delaware v. Continental Land Title Co.*,<sup>232</sup> the court held that a conditional use permit, requiring at least one occupant to be at least sixty-two years old or physically handicapped, should have been reported in the abstract of title because it was an encumbrance affecting title.<sup>233</sup> Also, in *Hopkins v. Lawyers Title Ins. Corp.*,<sup>234</sup> the court held that an agreement recorded in the county office of a probate judge, where the agreement was between a developer and a municipality regarding the liability for floods, was an encumbrance under the title insurance policy issued.<sup>235</sup>

Conversely, in *Bear Fritz Land Co. v. Kachemak Bay Title Agency, Inc.*,<sup>236</sup> a federal wetlands permit was not an encumbrance on title under the policy issued.<sup>237</sup> The Alaska court relied on its decision in *Domer*,<sup>238</sup> stating that "[a]s with the building and fire code violations in Domer, the wetlands designation here is not an encumbrance: it does not give any third person a right to or interest in the property, nor does it burden the property with a lien, interest or servitude."<sup>239</sup> The court distinguished between encumbrances affecting marketable title and defects solely changing the market value, in which the wetlands permit expiration fell into the latter

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<sup>232</sup> 20 Cal. Rptr. 2d 438 (Ct. App. 1993).

<sup>233</sup> *Id.* at 440-41.

<sup>234</sup> 514 So. 2d 786 (Ala. 1986).

<sup>235</sup> *Id.* at 787, 789.

<sup>236</sup> 920 P.2d 759 (Alaska 1996).

<sup>237</sup> *Id.* at 761-62.

<sup>238</sup> *Id.* at 762.

<sup>239</sup> *Id.*

category.<sup>240</sup>

In *Aldrich v. Hawrylo*,<sup>241</sup> the court held that a setback requirement on an unfilled subdivision plan did not affect title.<sup>242</sup> The New Jersey court found that “[t]itle insurance policies generally exclude from coverage the exercise of police power over matters of land use, land division and building because such matters are said not to be matters affecting title.”<sup>243</sup>

Whether certain encumbrances should be included in a title insurance policy widely varies, as case law suggests. It appears that some courts hold that an “encumbrance” parallels the “encumbrance” for purposes of marketable title and the covenant against encumbrances, while other courts define “encumbrance” solely for purposes of a title insurance policy, independent of its effect on title.

An extensive review of cases dealing with whether an insurance company is held liable for failing to report a permit, violation of ordinance, and so forth, in an abstract of title, is not entirely crucial for this Comment. This is because a title insurer’s liability depends largely upon the contract, which varies. Yet, the standard title insurance policy excludes losses that arise from the governmental police power.<sup>244</sup> Although regulations and ordinances arising out of the legislature’s police power are excluded, the

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<sup>240</sup> *Id.* at 761.

<sup>241</sup> 656 A.2d 1304 (N.J. 1995).

<sup>242</sup> *Id.* at 1308-09.

<sup>243</sup> *Id.* at 1309. Interestingly, however, an Illinois court held that if a lawsuit is pending regarding zoning violations, the title company has a duty to disclose such suit because it would render the title unmarketable. *Radovanov v. Land Title Co. of America Inc.*, 545 N.E.2d 351, 354 (Ill. App. Ct. 1989).

<sup>244</sup> Beverly J. Quail & Gwendolyn C. Allen, *Title Insurance Treatment of Zoning-Related Regulations and the ALTA Zoning Endorsement*, 30 COLO. LAW. 89 (2001).

exclusion does not apply when there is notice of a defect, lien or encumbrance resulting from a violation or alleged violation that affects the land.<sup>245</sup> This is contingent upon the notice being recorded in the public records.<sup>246</sup>

If there is a lack of notice due to unrecorded regulations, and a party builds in violation of the regulations, the title company will not be held liable.<sup>247</sup> Likewise, housing code violations, violations of subdivision regulations, certificate of occupancy violations, denial of permits, effects of environmental ordinances, and violations of municipal ordinances are excluded from coverage due to the lack of notice in records.<sup>248</sup> Given this exhaustive list, the municipal and governmental police power should do more to require recordings of violations, which could provide constructive notice to an innocent purchaser. If more were required to be recorded, the “public records” exclusion to the exception of coverage, which is typically seen in title insurance policies, would encompass more information that could provide a buyer with notice. This was discussed in the concurring opinion of *Bianchi*.<sup>249</sup> Chief Justice Allen of the Supreme Court of Vermont pointed out that municipalities do not, nor are they required to, record certificates of occupancy.<sup>250</sup> Therefore, when a seller, buyer or title examiner searches for encumbrances, each may search

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<sup>245</sup> *Id.*

<sup>246</sup> *Id.*

<sup>247</sup> *Id.* at 89-90.

<sup>248</sup> *Id.* at 90.

<sup>249</sup> *Bianchi*, 701 A.2d at 1037 (Allen, C.J., concurring).

<sup>250</sup> *Id.* at 1042.

for municipal records that do not even exist.<sup>251</sup> Chief Justice Allen described well the problems inherent, not only in Vermont, but in many jurisdictions that do not have well kept recording statutes.

Additionally, the term “encumbrance,” for purposes of the covenant against encumbrances, should mean the same thing for purposes of “encumbrance” in a title report. These inconsistencies might allow title insurance companies to avoid liability by failing to report violations, which might be a result of the poor records kept in some localities.

In sum, the departure from the caveat emptor rule shows that courts are sympathetic to purchasers when sellers possess greater knowledge about the property. However, those jurisdictions that have not entirely absolved the caveat emptor rule often leave purchasers unprotected, and seeking relief from misrepresentation is often difficult to prove. Similarly, a claim against a title insurance company may not provide a purchaser with relief because of the difficulty in proving reliance. While courts have moved in the direction to protect purchasers, for purposes of violations of zoning ordinances, the covenant against encumbrances and marketable title guarantee has not been expanded to protect purchasers. Likewise, misrepresentation law is insufficient to aid innocent purchasers. Lastly, the law regarding claims by a purchaser against a title insurance company is vague. Whether encumbrances such as zoning violations are required to be reported in the title report is unclear, which may be due to the fact that reporting requirements are similarly

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<sup>251</sup> *Id.* at 1043.

vague. What is required of a title insurance company depends on the jurisdiction, but from the illustration of the case law in section C, it is clear that there are many discrepancies and recovery from a title insurance company might be problematic.

Also, before arriving at the presumption that a buyer is solely responsible to discover a violation, one of the questions that must be asked is who is in the best position to guard against the risk of loss? When a seller has undergone building or construction of some sort, and throughout the process discovers or knows of a violation, the seller should have the duty to disclose this to a subsequent purchaser. Purchasers must be aware that often a seller will have no duty to disclose violations, and that they need to protect themselves by seeking assurances from the sellers. This will be discussed in Part V, as well as how the law, in the future, can better protect purchasers.

## **V. HOW A PURCHASER CAN BE PROTECTED IN THE FUTURE**

Part V explores what can be done in the future in terms of requiring more of a seller to disclose violations and how a purchaser can protect him or herself. Further, Part V considers the implied warranty of lawful use, an avenue that may be able to remedy the problems in this area.

As previously explained, the courts and legislatures substantially overruled the caveat emptor doctrine. Yet, sellers generally do not have a duty to disclose violations of zoning ordinances. This supports the proposition that the covenant against encumbrances and marketable title claims should not be limited. The rationale behind this is that if sellers are required to make more

disclosures, then they should be gaining more information about existing encumbrances, including zoning violations. Information regarding the lawful use of their property provides sellers with the information that they could disclose or be required to disclose to purchasers. By holding that violations of zoning ordinances, even latent violations, are encumbrances for purposes of the covenant against encumbrances, then sellers will be more willing to remedy the violations and avoid future violations.

**A.      Sellers Must Disclose Violations of Zoning Ordinances and Regulations to Innocent Purchasers**

Again, the caveat emptor rule does not provide a duty to disclose zoning ordinance violations.<sup>252</sup> There exists no special fiduciary relationship between a buyer and a seller such that the seller must disclose zoning ordinances.<sup>253</sup> Yet the seller is in a better position to “know of violations or detect them.”<sup>254</sup> For example, in *Bear Fritz*,<sup>255</sup> the sellers obtained a wetlands permit, failed to record it, and knew it would expire in three years.<sup>256</sup> A simple disclosure when selling to the buyers would have prevented the confusion for the buyers when the permit expired. Similarly, in *Fahmie*,<sup>257</sup> the seller, having knowledge of the culvert, could have informed the

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<sup>252</sup> See *supra* Part III.A; see also *Levin v. Kissena Manor Corp.*, 184 N.Y.S.2d 863, 866 (Sup. Ct. 1959), *aff'd*, 199 N.Y.S.2d 408 (App. Div. 1960).

<sup>253</sup> See *Levin*, 184 N.Y.S.2d at 866.

<sup>254</sup> Freyfogle, *supra* note 14, at 51.

<sup>255</sup> See *supra* notes 236–40 and accompanying text.

<sup>256</sup> *Bear Fritz*, 920 P.2d at 760.

<sup>257</sup> See *supra* notes 94–103 and accompanying text.

buyer that the culvert was defective in size and a violation of the Bureau of Water Control<sup>258</sup> requirements.

The caveat emptor doctrine should be abandoned entirely. Those jurisdictions that have not abandoned the caveat emptor rule or have property disclosure statutes that provide sellers with a way out should require more of sellers. If sellers were required to disclose violations of zoning ordinances, then ordinances in effect would be enforced and complied with. It seems “counter-intuitive that a purchaser can potentially be held liable for a violation that is not apparent. The loss should fall on the party who caused the violation and not the innocent party.”<sup>259</sup> The *Bianchi* court agreed when it stated, “the owner must bring the property into zoning compliance by meeting zoning permit requirements for an occupancy permit.”<sup>260</sup>

Purchasers should seek to protect themselves by employing the following, which the courts and legislature should seek to validate and impose: (1) contract provisions where sellers promise to disclose violations of ordinances and regulations; (2) affirmative representations from sellers; and (3) assurances from zoning authorities. First, while sellers should be required to disclose more concerning zoning violations, adding a provision in the contract that requires a seller to represent to the purchaser any violations of a zoning ordinance could guard against this. A buyer should “seek representations from its seller regarding compliance with zoning matters and insist on disclosure of any unrecorded restrictions

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<sup>258</sup> *Fahmie*, 408 A.2d at 791.

<sup>259</sup> Forman, *supra* note 3, at 818-19 (footnotes omitted).

<sup>260</sup> *Bianchi*, 701 A.2d at 1041.

relating to the property.”<sup>261</sup>

[W]here the contract contains a provision whereby the seller warrants and represents that, upon purchase, the property and its structures will not be in violation of any zoning ordinance or regulation[,] . . . [and] where it reasonably appears that the [purchaser] will be plagued by zoning problems when he purchases the property, a title defect does exist and the [purchaser] is entitled to demand that the [seller] rectify the same or return any moneys paid on account.<sup>262</sup>

In *Pamerqua Realty Corp. v. Dollar Service Corp.*,<sup>263</sup> a sales contract provided that “premises are sold and are to be conveyed subject to . . . zoning regulations and ordinances of the city, town or village in which the premises lie which are not violated by existing structures.”<sup>264</sup> Because the contract included the provision, it protected the purchaser from any zoning violations.<sup>265</sup>

Second, it is crucial that a buyer puts in a provision that warrants that the property is not in violation of any zoning ordinance or regulation. Buyers “truly have to keep their eyes wide open as they are considered to have entered into the sales contract with the knowledge that the property will be subject to zoning regulations and ordinances.”<sup>266</sup>

Another option for a purchaser is to tell the seller what his

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<sup>261</sup> Quail, *supra* note 244, at 91.

<sup>262</sup> Forman, *supra* note 3, at 816 (quoting *Pamerqua Realty Corp. v. Dollar Serv. Corp.*, 461 N.Y.S.2d 393, 395 (App. Div. 1983)).

<sup>263</sup> *Pamerqua Realty Corp.*, 461 N.Y.S.2d 393.

<sup>264</sup> *Id.* at 394.

<sup>265</sup> *Id.* at 395.

<sup>266</sup> Forman, *supra* note 3, at 820.

intended use of the property is and get a statement from the seller that this use will comply with zoning ordinances. “[T]o insert in the contract a stipulation stating the purposes for which the purchaser intends to use the property and to obtain from the seller a representation that the zoning ordinance does not prevent such intended use of the property”<sup>267</sup> would help a purchaser in a claim of misrepresentation.

Finally, buyers should also obtain a survey “with a certification regarding zoning matters and, where available, a letter from local zoning authorities addressing zoning classifications and restrictions on development.”<sup>268</sup> This will allow buyers to determine whether any latent violations exist.

Protecting against loss through contract provisions, seeking affirmative representations from sellers, and obtaining assurances from zoning authorities are all very important. However, there is a concern that “ ‘the unknowing buyer of property that violates some land use restraint’ ” will not protect himself.<sup>269</sup> That is why a buyer relies on a title insurance company<sup>270</sup> and his or her attorney. Attorneys should check zoning ordinances and whether they are being complied with before a purchaser is conveyed a certain piece of property.<sup>271</sup> Legal malpractice is possible where there has been a failure to adequately protect a buyer in this type of situation.<sup>272</sup>

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<sup>267</sup> *Id.* at 821.

<sup>268</sup> Quail, *supra* note 244, at 91.

<sup>269</sup> Forman, *supra* note 3, at 818.

<sup>270</sup> *See supra* Part IV.C.

<sup>271</sup> Forman, *supra* note 3, at 822.

<sup>272</sup> *Id.*

### B.      An Implied Warranty of Lawful Use

The best remedy to the current problem would be the creation of a new implied warranty of lawful use to better protect buyers. The new implied warranty should require the seller to warrant that the existing uses of the property and any other uses described by the seller must comply with the land use ordinances and regulations.<sup>273</sup> This warranty has been especially encouraged by Professor Eric T. Freyfogle,<sup>274</sup> who said the following:

Many courts, it is clear, are dissatisfied today with the application of the caveat emptor doctrine to real estate sales. They have expressed their dissatisfaction by seizing upon a variety of theories that soften the doctrine's impact on unsuspecting and poorly advised buyers. The theories by these courts, however, all suffer from multiple inadequacies. These inadequacies can be best resolved, and the caveat emptor rule best altered, through an approach not yet used expressly by any court: the judicial development of an implied warranty in all real estate sales contracts that existing property and other uses described by the seller comply with applicable land use restraints.<sup>275</sup>

The warranty would be part of the contract,<sup>276</sup> and would “restore contract law as the framework of seller-buyer dispute resolution.”<sup>277</sup> It would revolve around the disclosure of the

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<sup>273</sup> Freyfogle, *supra* note 14, at 4; *see also* Forman, *supra*, note 3, at 818.

<sup>274</sup> Eric T. Freyfogle is the Max L. Rowe Professor of Law at the University of Illinois College of Law, where for the past twenty years he has taught courses on property, natural resources, wildlife law, land use planning, and environmental law. Professor Freyfogle received his J.D. degree, *summa cum laude*, from the University of Michigan Law School.

<sup>275</sup> Freyfogle, *supra* note 14, at 32-33.

<sup>276</sup> *Id.* at 33.

<sup>277</sup> *Id.* at 5.

specifications of the property's characteristics and uses.<sup>278</sup> The warranty would impose a duty on the seller to identify the ordinances and regulations to determine if they are being violated.<sup>279</sup> By shifting the duty placed on the buyer to the seller, it would improve the compliance and correction of violations,<sup>280</sup> and, as a result, the governmental police power in maintaining the health, safety, and general welfare of the public would be indirectly enforced.

Two of the benefits that could potentially result from adopting an implied warranty of lawful use are: (1) it could relieve claims of misrepresentation arising out of tort law when the tort elements have been manipulated for the purpose of helping an innocent buyer;<sup>281</sup> and (2) it could encourage parties to comply with land use regulations, zoning ordinances, and building codes.<sup>282</sup> In terms of tort recovery, "the warranty provides a broader recovery and eliminates the troublesome issues of knowledge and scienter, materiality, and actual, reasonable reliance."<sup>283</sup> In terms of the covenant against encumbrances and marketability of title, buyers, even "unsuspecting and poorly advised buyers" could rely on the contract provision that would warrant the existing uses of the property are lawful.<sup>284</sup> The duty on sellers would also be more clear

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<sup>278</sup> *Id.* at 33.

<sup>279</sup> *Id.*

<sup>280</sup> Freyfogle, *supra* note 14, at 35.

<sup>281</sup> *See supra* notes 203-08 and accompanying text.

<sup>282</sup> Freyfogle, *supra* note 14, at 35.

<sup>283</sup> *Id.* at 34.

<sup>284</sup> *Id.* at 32. *See supra* note 275 and accompany text; *see also* Forman, *supra* note 3, at 818 (suggesting that an implied warranty of lawful use would also be helpful in the area of the covenant against encumbrances and marketable title area). The benefits of an implied warranty of lawful use are that:

and finite.

The warranty of habitability was created in an attempt to protect purchasers at a time when the caveat emptor doctrine prevailed.<sup>285</sup> Other warranties that have recently been created are the warranties of fitness and workmanlike constructions.<sup>286</sup> The courts have been willing to create new warranties where needed as the real estate market evolves.<sup>287</sup> Courts have suggested that it is the seller's duty to make sure that the property to be conveyed is complying with existing zoning ordinances and similar regulations.<sup>288</sup> As seen in *Bianchi*, the court stated a seller should be sure that he has the required permit in order to obtain a certificate of occupancy.<sup>289</sup> Similarly, in *Iverson v. Solsbery*,<sup>290</sup> the Colorado Court of Appeals stated that landowners owe a duty to future owners not to reconstruct property in violation of building codes.<sup>291</sup> It seems that the next logical step is to create an implied warranty of lawful use, just as the courts have created the warranty of habitability.

The scope of the warranty does not necessarily have to apply

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[An] implied warranty of lawful use would better protect the legitimate expectations of buyers, would greatly simplify the factual disputes in litigation, and would provide greater commercial certainty and flexibility for sellers by defining more precisely their responsibilities to buyers.

*Id.*

<sup>285</sup> See *supra* note 175 and accompanying text (discussing Colorado as the first to reject the doctrine of caveat emptor and apply a warranty of habitability).

<sup>286</sup> Freyfogle, *supra* note 14, at 36.

<sup>287</sup> *Id.*

<sup>288</sup> *Id.* at 37.

<sup>289</sup> See *supra* notes 161-62 and accompanying text.

<sup>290</sup> 641 P.2d 314 (Colo. 1982).

<sup>291</sup> *Id.* at 316.

solely to residential property. The need for compliance in land use restrictions applies equally to commercial and noncommercial property, and thus the warranty could apply to both.<sup>292</sup> The warranty should include “not only existing land uses, but any other uses that the seller specifically identifies or describes.”<sup>293</sup> In other words, if the seller makes assertions about the property, those become express warranties.<sup>294</sup> Next, it is a possibility that the parties by agreement could alter the warranty.<sup>295</sup>

Moreover, an implied warranty of lawful use will become increasingly necessary as courts continue to expand the doctrine of misrepresentation in tort law and hold sellers liable.<sup>296</sup> The vague area of the law surrounding misrepresentation among sellers could be better solved if there was a clearer requirement in what a seller had to represent to a potential buyer.

Again, sellers have more knowledge of the property including its uses and violations of land use restraints.<sup>297</sup> “The seller also will often possess property surveys and title abstracts and will have greater time and opportunity to learn of the legality of existing uses. . . . [H]is single study is more efficient than requiring all potential buyers to repeat and thus wastefully duplicate this inquiry.”<sup>298</sup> In sum, an implied warranty of lawful use would help protect buyers, as

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<sup>292</sup> Freyfogle, *supra* note 14, at 41.

<sup>293</sup> *Id.*

<sup>294</sup> *Id.*

<sup>295</sup> *Id.* at 42.

<sup>296</sup> *Id.* at 16.

<sup>297</sup> Freyfogle, *supra* note 14, at 19.

<sup>298</sup> *Id.*

well as simplify the factual investigation involved in litigation, and most importantly, it would define more precisely the duties a seller has to a buyer.<sup>299</sup>

## VI. CONCLUSION

In conclusion, the covenant against encumbrances and marketable title has had some discrepancies, which are of concern to purchasers, unaware of violations of existing municipal zoning ordinances at the time of conveyance. Courts generally hold that latent violations and violations of building codes do not constitute an encumbrance for purposes of the covenant against encumbrances and marketable title claims. Therefore, a purchaser is without a means of rescission or damages. Often times the seller has greater knowledge about the existing uses of the property and any violations. However, the doctrine of caveat emptor, although it is rejected in the majority of jurisdictions, still leaves buyers unprotected because there is no duty to disclose violations of zoning ordinances.

Courts must not limit the scope of the covenant against encumbrances and marketability of title, rendering them meaningless when there is a latent violation. Purchasers can seek to protect themselves through the contract or by seeking representations from the seller. But most importantly, an implied warranty of lawful use is greatly needed to alleviate failed misrepresentation claims and fill in the gaps when there is a latent violation of a zoning ordinance. In addition, an implied warranty of lawful use would resolve buyer-

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<sup>299</sup> Forman, *supra* note 3, at 818.

seller disputes and specifically lay down the requirements of sellers. It is the hope of many buyers that the property they are buying is in compliance with any zoning ordinances or land use regulations. Thus, the courts should recognize the need for an implied warranty of lawful use.