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An Update on Contract Damages When the Landlord Breaches the Implied Warranty of Habitability: *Surratt v. Newton* and *Allen v. Simmons*

By enacting the Residential Rental Agreements Act in 1977, the North Carolina General Assembly established an implied warranty of habitability in residential leases. The Act, however, does not specify the damages that a tenant may recover if her landlord violates the implied warranty. Ten years after the enactment of the statute, in *Miller v. C.W. Myers Trading Post*, the North Carolina Court of Appeals adopted a “benefit of the bargain” formula for computing such damages. This measure of damages seeks to put the plaintiff in the position she would have attained if the defendant had performed his contract duty.

In *Surratt v. Newton* and *Allen v. Simmons* the court of appeals added substance to the structure it had established in *Miller*. Most notably, the court placed a “rent paid” ceiling on the *Miller* formula for damages; defined the contract rights of tenants who ceased paying rent before vacating their rental units; and held that the actions of the breaching landlord may constitute unfair trade practices, for which the landlord may be liable for treble damages.

This Note examines the court’s opinions in *Surratt* and *Allen* in light of judicial precedent and the Residential Rental Agreements Act. The Note concludes that the holdings are reasonable, although not clearly expressed. The Note then offers three principles to guide future holdings, focusing primarily on reducing the uncertainty surrounding legal liability in this area.

Plaintiff Katherine Surratt rented a house in Winston-Salem, North Carolina from 1974 or 1975 through March 1987. Defendant Jerry Newton was the rental agent and property manager responsible for the house during the last fourteen months of her tenancy. Plaintiff alleged that defendant failed to respond to her many requests for repairs of defective conditions existing in the house. Plaintiff alleged that defendant failed to respond to her many requests for repairs of defective conditions existing in the house.

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4. Id. at 371, 355 S.E.2d at 194.
8. Id. at 642, 394 S.E.2d at 482; *Surratt*, 99 N.C. App. at 407, 393 S.E.2d at 560.
11. *Surratt*, 99 N.C. App. at 399, 393 S.E.2d at 556.
12. Id. at 400, 393 S.E.2d at 556. For Ms. Surratt's entire tenancy before 1986, Paul Jeffrey Newton, d/b/a Newton Brothers, was the rental agent. He was also a defendant in Surratt's suit, but the trial court dismissed his appeal based on his failure to file a notice of appeal within ten days of the judgment. The court of appeals affirmed this dismissal. Id. at 400-03, 393 S.E.2d at 556-58.
house throughout her occupancy. These conditions included "electrical failures, flooding of sewage and water into the house, rodent infestation, and other deteriorating conditions throughout the house." Plaintiff ceased paying rent in November 1986, which precipitated a summary ejectment action by defendant. The court entered judgment against plaintiff, and she vacated the premises at the end of February or the beginning of March of 1987.

In March 1987 Surratt appealed to the district court for a trial de novo and filed an answer asserting that she owed no rent because the defendants had failed to maintain the premises in a safe and habitable condition. In addition to moving to dismiss the summary ejectment claim, plaintiff counterclaimed for rent abatement and other consequential and actual damages. Defendant voluntarily dismissed the summary ejectment action and moved for summary judgment on plaintiff's counterclaims, but the court denied the motion and plaintiff prevailed on the merits of the counterclaims. Defendant then appealed to the North Carolina Court of Appeals.

Newton's appeal raised several issues concerning the nature and extent of landlord liability under the Residential Rental Agreements Act. Judge Eagles, writing for the court, first defined the extent of damages that a tenant can receive in a rent abatement action. The court disagreed with defendant's contention

Ms. Surratt reached a settlement with the owners of the rental house, who were also defendants in the original action. Id. at 399, 393 S.E.2d at 556.

13. Id. at 400, 393 S.E.2d at 556.

14. Id.

15. Id.

16. Id.

17. Id.

18. Id.

19. Id. at 400-01, 393 S.E.2d at 556.

20. Id. at 401, 393 S.E.2d at 557.

21. The Residential Rental Agreements Act provides in relevant part:

(a) The landlord shall:

(1) Comply with the current applicable building and housing codes, whether enacted before or after October 1, 1977, to the extent required by the operation of such codes; . . .

(2) Make all repairs and do whatever is necessary to put and keep the premises in a fit and habitable condition;

(3) Keep all common areas of the premises in safe condition; and

(4) Maintain in good and safe working order and promptly repair all electrical, plumbing, sanitary, heating, ventilating, air conditioning, and other facilities and appliances supplied or required to be supplied by him provided that notification of needed repairs is made to the landlord in writing by the tenant except in emergency situations.


The court also rejected defendant Newton's argument that he was not a proper defendant. Surratt, 99 N.C. App. at 403-05, 393 S.E.2d at 558-59. The court held that Newton was a "landlord," defined for the purposes of the Act as "any owner and any rental management company, rental agency, or any other person having the actual or apparent authority of an agent to perform the duties imposed by this Article." N.C. GEN. STAT. § 42-40(3) (1984). The court distinguished the case from its earlier holding in Collingwood v. General Elec. Real Estate Equities, 89 N.C. App. 656, 659, 366 S.E.2d 901, 903 (1988), rev'd in part on other grounds, 324 N.C. 63, 376 S.E.2d 425 (1989), that a property manager is not liable for defects in design and construction. Surratt, 99 N.C. App. at 404-05, 393 S.E.2d at 558-59.
that he was liable for no more than the amount of his rental commission. Instead, the court based the damages recoverable on the damages formula it had adopted in Miller:

"[A] tenant may recover damages in the form of a rent abatement calculated as the difference between the fair rental value of the premises if as warranted (i.e. in full compliance with G.S. 42-42(a)) and the fair rental value of the premises in their unfit condition for any period of the tenant's occupancy during which the finder of fact determines the premises were uninhabitable, plus any special or consequential damages alleged and proved." The court qualified this rent abatement formula, however, by declaring that "the amount of rent paid is a limit on recovery." Thus, the Surratt court employed a literal reading of Miller, which had found a cause of action "for recovery of rent paid." Thus, a more precise statement of the rent abatement formula is: the lesser of (1) fair rental value as warranted less fair rental value "as is," and (2) the rent paid during the period that the premises were uninhabitable.

In addition, the Surratt court addressed the nature of the tenant's responsibilities in the following three aspects of a rent abatement claim: The requirement of notice to the landlord concerning defective conditions; the evidence used to establish fair rental values; and the consequence of withholding rent. Defendant argued that a tenant cannot recover for defects that fall under section 42-42(a)(4), which includes "electrical, plumbing, sanitary, heating, ventilating, air conditioning, and other facilities and appliances," if she has failed to provide the landlord with the written notice required under that subsection. The court rejected that argument, noting that the jury had found that the orally requested repairs were needed to put the house in "fit and habitable condition." Because section 42-42(a)(2), which requires the landlord to "put and keep the premises in a fit and habitable condition," does not explicitly require written notice from the tenant, the court held that "where the conditions enumerated in G.S. 42-42(a)(4) are the same conditions that render the premises unfit and uninhabitable no written notice is required under the statute."

Defendant next argued that the damages awarded were contrary to the evidence of fair market value produced at trial. In response, the court noted that defendant himself had testified that the house had a fair rental value of $600 per

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22. Surratt, 99 N.C. App. at 406-07, 393 S.E.2d at 560 ("No lesser measure of damages is recoverable against a landlord (as defined by G.S. 42-40(3)) merely because he is not the owner but is an agent.").

23. Id. at 406, 393 S.E.2d at 560 (quoting Miller v. C.W. Myers Trading Post, 85 N.C. App. 362, 371, 355 S.E.2d 189, 194 (1987)).

24. Id.

25. Id. at 407, 393 S.E.2d at 560 (quoting Miller, 85 N.C. App. at 368, 355 S.E.2d at 193).


27. Surratt, 99 N.C. App. at 405, 393 S.E.2d at 559.

28. Id.


30. Surratt, 99 N.C. App. at 405-06, 393 S.E.2d at 559.

31. Id. at 408, 393 S.E.2d at 561. Specifically, he contended that plaintiff had failed to prove that the fair rental value of the house was different from the amount of rent charged. Id.
month and that "it only rented for less because of the nature of the neighborhood." The court held the testimony to be sufficient for the jury to determine damages.33

Finally, the court agreed with defendant that the jury could not award rent abatement damages for the period that plaintiff had withheld rent payments, although it rejected his rationale for this conclusion.34 Defendant argued that the Residential Rental Agreements Act's provision that "[t]he tenant may not unilaterally withhold rent prior to a judicial determination of a right to do so" precluded rent abatement during the period of rent withholding. Instead of accepting this argument, the court simply characterized rent abatement as a refund of all or part of rent actually paid and held, in effect, that one cannot refund an amount never paid.36 The court noted, however, that there is "nothing in the Act" to preclude entirely a tenant from collecting damages because she withholds rent; she just may not collect damages for the period of the withholding.37

Significantly, the Surratt court split on the fundamental question of exactly how rent abatement relates to an action for breach of the warranty of habitability. Judge Eagles distinguished an action for rent abatement from an action for breach of the warranty of habitability.39 He stated, "Since the pleadings here pray for relief in rent abatement and do not seek damages for breach of the covenant of habitability, we expressly decline to address here the issue of whether damages for the breach of a covenant of habitability are limited to the amount of rent paid." Judge Greene, who concurred in the result, took issue with the court's "suggestion . . . that an action in rent abatement somehow differs from an action for breach of warranty for habitability." He characterized rent abatement as only one of the remedies available for a breach of the warranty of habitability.40

In Allen the court of appeals reviewed a fact pattern similar to that in Surratt. Defendant Warnell Simmons rented a house from Scott Realty, the agent for plaintiff Harvey Allen, after Scott Realty allegedly agreed to make specified

32. Id.
33. Id.
34. Id. at 407, 393 S.E.2d at 560.
37. Id.
38. Id. In an opinion concurring in the result, Judge Greene went further in explaining the position of a tenant who has withheld rent in response to the landlord's failure to provide fit premises. Judge Greene stated that such a tenant, as a defendant in a summary ejectment action, can seek an abatement of rent due. Under those circumstances, however, Judge Greene would modify the court's rent abatement formula by replacing the "as warranted" term with "agreed rent." Id. at 411, 393 S.E.2d at 562 (Greene, J., concurring in result).
39. Id. at 409, 393 S.E.2d at 561.
40. Id.
41. Id. at 411, 393 S.E.2d at 562 (Greene, J., concurring in result).
42. Id. (Greene, J., concurring in result). Judge Greene identified special and consequential damages as two other remedies for a breach of the warranty. Id. (Greene, J., concurring in result).
repairst prior to occupancy. Defendant alleged that Scott Realty failed to make the repairs before she moved into the house in November 1985 and failed to correct defects brought to its attention throughout her tenancy. Simmons occupied the house until July 1987, although she ceased paying rent after August 1986. Defendant’s initial rent withholding occurred concurrently with the Winston-Salem Housing Services Department’s declaration, issued on September 5, 1986, that the house was unfit for human habitation.

Allen brought a summary ejectment action and prevailed in an April 1987 hearing in magistrate’s court. Defendant then appealed to the district court and, in addition, counterclaimed for rent abatement and damages for fraud, intentional infliction of emotional distress, and unfair and deceptive trade practices. The district court entered directed verdicts on all of the counterclaims against the defendant, and she appealed. The court of appeals affirmed the trial court’s directed verdicts on the fraud and intentional infliction of emotional distress counterclaims, but reversed the trial court on the other counts, finding sufficient evidence to reach the jury on the rent abatement and unfair trade practice claims.

In the majority opinion, Judge Eagles reiterated his Surratt position that, section 42-44(c) notwithstanding, a tenant’s withholding of rent does not bar him from recovering damages, except rent abatement for the period of withholding. His discussion of rent abatement, including the formula for determining damages, mirrored his Surratt opinion. Judge Eagles again distinguished between an action for rent abatement and an action for breach of the implied war-

43. Allen, 99 N.C. App. at 638, 394 S.E.2d at 480. “The defects included: holes in some of the walls; a damaged faucet on the kitchen sink; electrical problems, plumbing that leaked in the bathroom and in the basement; a damaged commode; a damaged hot water heater; fleas; broken glass; and no furnace.” Id.

44. Id. These alleged ongoing problems included pipes bursting from lack of heat, rats entering through holes in the walls, and a fire caused by defective wires. The defendant testified that a furnace was not installed until the day before she vacated the house. Id. at 638-39, 394 S.E.2d at 480.

45. Id. at 638, 394 S.E.2d at 480.
46. Id. at 639, 394 S.E.2d at 480.
47. Id. at 638, 394 S.E.2d at 480.
48. Id.
49. Id. at 640, 394 S.E.2d at 481.
50. Id. at 643, 394 S.E.2d at 483 (finding “no evidence that at the time of his promise plaintiff intended not to make the repairs” he promised to make).
51. Id. at 646, 394 S.E.2d at 484 (finding no evidence of serious mental distress or other bodily harm).
52. Id. at 642, 394 S.E.2d at 482.
53. Id. at 645, 394 S.E.2d at 484. Unfair trade practices are addressed in N.C. GEN. STAT. § 75-1.1 (1988). Subsection (a) provides: “Unfair methods of competition in or affecting commerce, and unfair or deceptive acts or practices in or affecting commerce, are declared unlawful.” Id. § 75-1.1(a). The statute defines commerce broadly to include “all business activities,” id. § 75-1.1(b), although it expressly excludes services rendered by someone in a “learned profession” and certain activities of advertising media. Id. § 75-1.1(b), (c).
54. The Residential Rental Agreements Act provides that the “tenant may not unilaterally withhold rent.” N.C. GEN. STAT. § 42-44(c) (1984); see supra notes 35-38 and accompanying text.
55. Allen, 99 N.C. App. at 642, 394 S.E.2d at 482.
56. See id. at 641-42, 394 S.E.2d at 482; supra notes 22-40 and accompanying text.
ranty of habitability. Tenants may bring an action seeking damages for breach of the implied warranty of habitability and may also seek rent abatement for their landlord's breach of the statute," he stated.

The court also found that defendant had presented evidence from which a jury could find that plaintiff had committed an unfair trade practice under section 75-1.1. After determining that Simmons and Allen were proper parties to such an action, the court noted that Simmons provided evidence that plaintiff failed to respond to numerous notices concerning the unfit and uninhabitable condition of the house. The court placed special significance on the fact that, "[d]espite the unfit conditions of the house, Scott Realty attempted to collect rent." It found that "[Allen's] behavior [could] be considered 'immoral, unethical, oppressive, unscrupulous, or substantially injurious to consumers.'" Evidence that Simmons suffered additional expenses because of the unfit conditions was the final element cited by the court in finding that a jury should have determined the unfair trade practice issue.

Surratt and Allen are the latest chapters in North Carolina landlord and tenant law as it has evolved since the enactment of the Residential Rental Agreements Act in 1977. Prior to the Act, the common-law doctrine of caveat emptor applied to residential leases in North Carolina and absolved landlords of any duty to maintain and repair the leased premises. By the late 1970s, approximately one-third of the states had moved away from caveat emptor by judicial creation of landlord duties under an implied warranty of habitability. Also during this period, adoption of the Uniform Residential Landlord and Tenant Act (URLTA), which includes an implied warranty of habitability, established a statutory implied warranty in an equivalent number of states. Courts now

57. Allen, 99 N.C. App. at 641, 394 S.E.2d at 482.
58. Id.
59. Id. at 645, 394 S.E.2d at 484.
60. Id. at 644, 394 S.E.2d at 483. Plaintiff was a physician who owned the house rented by Simmons and retained Scott Realty as rental agent. Plaintiff-Appellee's Brief at 9, Allen (No. 8921DC1155). Dr. Allen argued that he was not in the business of real estate. Id. Finding Scott Realty to be in the business of real estate, however, the court used the concept of agency to find Allen to be a proper defendant in the unfair trade practice action. See Allen, 99 N.C. App. at 644, 394 S.E.2d at 483.
61. Allen, 99 N.C. App. at 644, 394 S.E.2d at 484.
62. Id. at 644-45, 394 S.E.2d at 484. "[P]laintiff even went to defendant's house in February 1987 in an effort to collect past due rent for the unfit house." Id.
63. Id. at 645, 394 S.E.2d at 484 (quoting Mosley & Mosley Builders, Inc. v. Landin Ltd., 97 N.C. App. 511, 517, 389 S.E.2d 576, 579, disc. rev. denied, 326 N.C. 801, 393 S.E.2d 898 (1990)).
64. Id.
67. See id. at 314.
69. R. SCHOSHINSKI, supra note 2, § 3:31, at 152.
recognize an implied warranty of habitability in residential leases in all but a handful of jurisdictions.\textsuperscript{70}

Generally, when a landlord breaches the implied warranty of habitability, the tenant is entitled to vacate the premises and terminate the lease.\textsuperscript{71} It is not necessary for a rental unit to be "literally uninhabitable" for a breach to occur.\textsuperscript{72} Thus, a tenant can seek relief for the landlord's breach while continuing in occupancy of an unfit unit, or she may seek relief after vacating the premises for the period during which she occupied the premises.\textsuperscript{73}

Courts have developed at least three different formulas to calculate the damages suffered by a tenant occupying an unfit rental unit.\textsuperscript{74} First, courts can measure the damages as the difference between the fair rental value of the premises as warranted and the fair rental value of the premises in their unfit condition, or "as is."\textsuperscript{75} This approach seeks to compensate the tenant for the loss of her bargain.\textsuperscript{76} Second, courts may compute the damages as the difference between the agreed rent and the "as is" fair rental value.\textsuperscript{77} This view effectively requires that the tenant pay the fair rental value of the defective premises.\textsuperscript{78} Third, the damages may be a percentage of the agreed rent representing the percentage reduction in the tenant's use and enjoyment of the premises resulting from the breach.\textsuperscript{79} In a modified version of the third formula, the court uses the "as warranted" and "as is" fair market values in computing the percentage to be applied to the agreed rent in calculating damages.\textsuperscript{80} When the court computes damages as a percentage of agreed rent, the resulting reduction in the rent obligation commonly is called a rent abatement.\textsuperscript{81}

In addition to collecting damages for the landlord's breach, the tenant may assert a breach of the implied warranty of habitability as a defense to an action for rent.\textsuperscript{82} This defense is a consequence of the tenant's right to terminate the lease following the landlord's breach,\textsuperscript{83} which precludes the landlord from collecting the full agreed rent during a period when unfit conditions constituting a

\textsuperscript{70} See \textit{id.} § 3:16, at 67 n.30 (Supp. 1990) (implied warranty of habitability not recognized by courts in Alabama, Florida, Idaho, Kentucky, Oregon, and South Carolina).

\textsuperscript{71} R. \textsc{Cunningham}, W. \textsc{Stoebuck} & D. \textsc{Whitman}, \textit{supra} note 66, § 6.41, at 333. This entitlement derives from the mutuality of landlord and tenant obligations under a lease. \textit{Id.} Termination of a lease in this manner is "very similar to a traditional 'constructive eviction' based on the landlord's failure to perform an express covenant to maintain the premises." \textit{Id.} at 333 n.3.

\textsuperscript{72} R. \textsc{Schoshinski}, \textit{supra} note 2, § 3:17, at 68 (Supp. 1990).

\textsuperscript{73} See \textit{id.}

\textsuperscript{74} R. \textsc{Cunningham}, W. \textsc{Stoebuck} & D. \textsc{Whitman}, \textit{supra} note 66, § 6.42, at 336.

\textsuperscript{75} R. \textsc{Schoshinski}, \textit{supra} note 2, § 3:25, at 141-42.

\textsuperscript{76} \textit{Id.} at 141.

\textsuperscript{77} \textit{Id.} at 142.

\textsuperscript{78} \textit{Id.}

\textsuperscript{79} R. \textsc{Cunningham}, W. \textsc{Stoebuck} & D. \textsc{Whitman}, \textit{supra} note 66, § 6.42, at 337.

\textsuperscript{80} R. \textsc{Schoshinski}, \textit{supra} note 2, § 3:25, at 142-43. It is not obvious that this modified formula produces a different measure of damages than the formula it modifies.

\textsuperscript{81} \textit{Id.} Rent is abated when damages constitute an effective refund of prior rent payments or when a tenant who has withheld rent is relieved of the obligation to pay all or part of past due rent. \textsc{Black's Law Dictionary} 4 (6th ed. 1990).

\textsuperscript{82} R. \textsc{Schoshinski}, \textit{supra} note 2, § 3:22, at 136.

\textsuperscript{83} See \textit{supra} note 71 and accompanying text.
breach exist. Indeed, in the landmark implied warranty case of Javins v. First National Realty Corp., the United States Court of Appeals for the District of Columbia Circuit went even further and held that a breach-of-implied-warranty defense could be used not only in an action for nonpayment of rent, but also in an action for possession.

The first recognition of an implied warranty of habitability in North Carolina was judicial. In 1974 the North Carolina Supreme Court held that such a warranty applies to the sale of newly constructed houses. The following year, however, the court of appeals refused to recognize an implied warranty of habitability in residential leases. The North Carolina General Assembly countered that decision by enacting the Residential Rental Agreements Act in 1977. The Act provides that the tenant’s obligations to pay rent and maintain clean premises and the landlord’s obligation to provide fit premises are mutually dependent. The landlord’s obligation includes specific responsibilities concerning building and housing code compliance, common-area maintenance, and maintenance of electrical and other facilities, and a general responsibility to “[m]ake all repairs and do whatever is necessary to put and keep the premises in a fit and habitable condition.” The statute does not delineate specific remedies, but provides that “[a]ny right or obligation declared by this Chapter is enforceable by civil action, in addition to other remedies of law and in equity.

Because the Act lacks specificity concerning a tenant’s remedies for landlord violations of the Act, the North Carolina Court of Appeals began filling the void. The initial cases before the court of appeals were tort actions involving personal injury and wrongful death. In those cases, the court found landlords to be in violation of the Act in instances of dimly lit steps in a common area, failure to repair steps of the rental unit, and failure to repair a heating flue.

84. R. Schoshinski, supra note 2, § 3:21, at 136.
86. Id. at 1082.
88. Id. (implied warranty that house is free of major structural defects and satisfies workman-like quality standard).
92. Id. § 42-42(a). For a further explanation of § 42-42(a), see supra note 21.
93. N.C. Gen. Stat. § 42-44(a) (1984). The other two provisions of this section, however, limit the right to recover for violations of the Act by providing that “[t]he tenant may not unilaterally withhold rent prior to a judicial determination of a right to do so” and that “[a] violation of this Article shall not constitute negligence per se.” Id. § 42-44(c), (d).
95. O’Neal, 55 N.C. App. at 228, 284 S.E.2d at 710.
96. Brooks, 57 N.C. App. at 559-60, 291 S.E.2d at 891.
97. Jackson, 73 N.C. App. at 369, 326 S.E.2d at 299.
In *Miller*,98 decided in 1987, the court of appeals first addressed the issue of contract remedies under the Residential Rental Agreements Act. The plaintiffs rented a house from defendant for over six years before bringing suit and sought recovery of rent paid for premises that defendant allegedly failed to maintain in a fit and habitable condition as required by the Act.99 In reversing the trial court's grant of summary judgment for defendant, the *Miller* court held that the Act provides "an affirmative cause of action to a tenant for recovery of rent paid based on the landlord's noncompliance with [section] 42-42(a)."100 The court based its damages formula on two premises. First, the court stated, "[t]he implied warranty of habitability entitles a tenant in possession of leased premises to the value of the premises as warranted, which may be greater than the rent agreed upon or paid."101 Second, the court ruled that a tenant in possession of defective housing is "liable only for the reasonable value, if any, of his use of the property in its defective condition."102 The court then declared the formula for damages "in the form of a rent abatement" to be the difference between the rental unit's fair rental value as warranted and its fair rental value "as is".103

In another 1987 case, *Cotton v. Stanley*,104 the court commented further on the application of the *Miller* formula for computing damages arising from a landlord's breach.105 The court held that the illegality of renting housing that violates a housing code does not automatically establish a fair market value of zero for such housing in possession of a plaintiff tenant.106 Dismissing the defendant's contention that plaintiffs must produce direct evidence of the two fair rental values in the damage formula, however, the court held that "[t]he fair rental value of property may be determined 'by proof of what the premises would rent for in the open market, or by evidence of other facts from which the fair rental value of the premises may be determined.'"107 The court found that the rent to which the parties agreed was nonbinding evidence of the fair rental value as warranted, and that the jurors' personal experience with housing together with descriptions of the premises from plaintiffs and a building inspector were sufficient for the jury to determine a fair rental value "as is".108 Thus,

99. *Id.* at 364-65, 355 S.E.2d at 190-91. For the landlord's maintenance obligations under the Act, see *supra* note 21.
100. *Miller*, 85 N.C. App. at 368, 355 S.E.2d at 193. The court stated that "[t]he action for a rent abatement for breach of an implied warranty is wholly contractual." *Id.* at 371, 355 S.E.2d at 195.
101. *Id.* at 370, 355 S.E.2d at 194. The court explicitly held that renting unfit housing at a "fair" rental value for that property would not free a landlord from obligations under the Residential Rental Agreement Act. *Id.*
102. *Id.* at 370-71, 355 S.E.2d at 194.
103. *Id.* at 371, 355 S.E.2d at 194; see *supra* note 23 and accompanying text.
105. The court of appeals also affirmed the right of a group of tenants to bring a class action for breach of the implied warranty of habitability. *Id.* at 539, 358 S.E.2d at 696.
106. *Id.* at 538, 358 S.E.2d at 695. "The measure of the unit's fair rental value is not the price at which the owner could lawfully rent the unit to a new tenant in the open market, but the price at which he could rent it if it were lawful for him to do so." *Id.*
107. *Id.* at 539, 358 S.E.2d at 695 (quoting *Brewington v. Loughran*, 183 N.C. 558, 565, 112 S.E. 257, 260 (1922)) (emphasis added in *Cotton*).
108. *Id.*
Cotton provided broad leeway regarding the evidence that a tenant can introduce for the valuation of damages under the Miller formula.

Any action potentially affecting the damages recoverable in a consumer suit may also involve a claim of unfair trade practices.\textsuperscript{109} The court of appeals has held that the rental of residential housing is in the nature of "trade or commerce" within the meaning of section 75-1.1 of the North Carolina General Statutes, the unfair trade practice statutes.\textsuperscript{110} In one case, a state district court judge found that the defendants committed an unfair trade practice when they "violated the North Carolina Residential Rental Agreements Act and the Tenant Security Deposit Act."\textsuperscript{111} The trial judge assessed damages of $240, which was the amount of the security deposit, and trebled the damages to $720.\textsuperscript{112}

In Surratt and Allen the North Carolina Court of Appeals added a rent-paid ceiling to its previously stated formula for contract damages arising from a landlord's violation of the implied warranty of habitability, while addressing for the first time the effect of rent withholding on the tenant's rights in an implied warranty action. The Surratt court established the rent paid by the tenant as a cap on the damages otherwise collectible under the court's "benefit of the bargain" formula.\textsuperscript{113} The court determined that it had prescribed such a cap by its prior characterization of a tenant's action as "recovery of rent paid."\textsuperscript{114}

The Surratt court's imposition of an agreed rent ceiling on the damages formula might have been influenced by the Miller court's use of the "rent abatement" label in the formula.\textsuperscript{115} Generally, rent abatement and benefit of the bargain measures are distinct implied warranty damage measures.\textsuperscript{116} One might view the court's new formula, however, as a merger of the two concepts. In this merger, the court has chosen to use agreed rent as a variable in the "rent abatement" formula while abandoning the "percentage of rent" damage measure nor-

\textsuperscript{109} N.C. GEN. STAT. § 75-1.1 (1988). The court will award treble damages when those damages result from an unfair trade practice. Id. § 75-16.


\textsuperscript{111} Borders v. Newton, 68 N.C. App. 768, 769, 315 S.E.2d 731, 731 (1984) (renting a dwelling that was under a condemnation order). The court of appeals dealt only indirectly with the unfair trade practice concept, ruling that the plaintiffs could not recover fraud damages because they had already recovered treble damages for the same conduct under the unfair trade practices statute. The court thereby implied that a violation of the Residential Rental Agreements Act could constitute an unfair trade practice. See id. at 770, 315 S.E.2d at 732.


\textsuperscript{112} Borders, 68 N.C. App. at 770, 315 S.E.2d at 731.

\textsuperscript{113} Surratt, 99 N.C. App. at 406, 393 S.E.2d at 560; see supra text accompanying notes 23-25.

\textsuperscript{114} Surratt, 99 N.C. App. at 407, 393 S.E.2d at 560 (quoting Miller v. C.W. Myers Trading Post, 85 N.C. App. 362, 368, 355 S.E.2d 189, 193 (1987)). To at least one commentator, however, such a conclusion is not inevitable. See Note, Miller v. C.W. Myers Trading Post: North Carolina Adopts Expansive Tenant Remedies for Violations of the Implied Warranty of Habitability, 66 N.C.L. REV. 1276, 1285 (1988) ("[T]he actual rent paid is not considered in the damage formula" in Miller.).

\textsuperscript{115} Miller, 85 N.C. App. at 366, 355 S.E.2d at 191; see supra text accompanying note 23.

\textsuperscript{116} See R. SCHOSHINSKI, supra note 2, § 3:25, at 141-43.
mally associated with rent abatement.\textsuperscript{117} If the "as warranted" rental value exceeds the agreed rent, the tenant might recover damages in excess of those awarded under a traditional rent abatement formula, but, as under traditional rent abatement, damages will not exceed the agreed rent.

Use of an "as warranted" benchmark in computing damages is consistent with the \textit{Miller} court's concept that the implied warranty of habitability gives the tenant a statutory entitlement to habitable premises.\textsuperscript{118} This recognition of the tenant's legitimate expectation interest\textsuperscript{119} parallels the Uniform Commercial Code's basic contract principle that "the aggrieved party [should] be put in as good a position as if the other party had fully performed."\textsuperscript{120} The "as warranted" measure of damages raises the possibility that the damages would exceed the agreed rent when the landlord and tenant agree to the rental of unfit housing at a rent significantly below the "as warranted" value.\textsuperscript{121} One might view this result as a reasonable consequence of renting unfit housing or, alternatively, as "the patently absurd result that the landlord would have to pay the tenant for occupying the unit."\textsuperscript{122} Under similar circumstances, a damage measure of agreed rent minus fair rental value "as is" would yield zero damages, "at least where the [unfit] condition of the dwelling unit has not worsened since the beginning of the tenancy."\textsuperscript{123} This result would appear to be a clear violation of section 42-42(b), which bars an explicit or implicit waiver of the implied warranty by the tenant.\textsuperscript{124}

The court's agreed-rent cap on the damage formula is a compromise between an unrestricted benefit of the bargain formula and a formula providing damages only to the extent that the "as is" value falls below the agreed rent. The court's seemingly flexible evidence requirements for proving fair rental values in \textit{Cotton}\textsuperscript{125} and \textit{Surratt}\textsuperscript{126} create for landlords uncertainty concerning their potential liability, even under the \textit{Surratt} compromise formula. To reduce this uncertainty by requiring expert testimony would add to the litigation costs of tenant-plaintiffs, many of whom have low incomes.\textsuperscript{127} The percentage diminution approach, a rent abatement damage measure based on the percentage reduction in use and enjoyment resulting from the landlord's breach applied to the agreed rent, eliminates much of the uncertainty and cost of using fair rental

\begin{footnotes}
\item[117] Id. at 142-43.
\item[118] See Miller, 85 N.C. App. at 370, 355 S.E.2d at 194 (the tenant is entitled to the as-warranted value of the leased housing).
\item[119] E. Farnsworth, supra note 5, § 12.1, at 840.
\item[120] U.C.C. § 1-106(1) (1989).
\item[121] R. Cunningham, W. Stoebuck & D. Whitman, supra note 66, § 6.42, at 338.
\item[122] Id.
\item[123] Id. at 337.
\item[124] N.C. Gen. Stat. § 42-42(b) (1984) ("The landlord is not released of his obligations under any part of this section by the tenant's explicit or implicit acceptance of the landlord's failure to provide premises complying with this section . . .").
\item[126] See Surratt, 99 N.C. App. at 408, 393 S.E.2d at 561; supra text accompanying notes 31-33.
\item[127] See R. Schoshinski, supra note 2, § 3:25, at 143.
\end{footnotes}
A broader perspective from which to evaluate damages for breach of the implied warranty of habitability would be that of public housing policy. One commentator, for example, has argued against adopting a percentage diminution approach by asserting that it would not discourage the practice of renting unfit housing at rents below as-warranted values. From a policy standpoint, the potential tradeoff resulting from alternative damage formulas rests between a higher rate of compliance with the implied warranty obligations, obtained by using a liberal damages formula, and a more ample stock of housing for low income persons, albeit with a lower warranty compliance rate, obtained through a damages formula rendering more modest awards. Because the Residential Rental Agreements Act is only one small piece in the array of federal, state, and local housing laws and programs, however, the North Carolina courts are better situated to apply contract law principles in fashioning a damages formula than to incorporate economic analysis of the housing market into their choice of remedies.

The extent to which the Surratt damages formula fills in the picture concerning tenant remedies for landlord breach is diminished further by Judge Eagles's distinction between rent abatement and damages for breach of implied warranty. Although Judge Greene appropriately criticized this distinction in his concurring opinion in Surratt, Judge Eagles stated the distinction in even stronger terms in his opinion for the Allen court. Perhaps Judge Eagles simply was referring to the concluding phrase of the Miller damage formula statement, which allowed, in addition to rent abatement, "any special or consequential damages alleged and proved." Subsequent opinions have quoted this provision, but an alternative interpretation of Judge Eagles's opinion is that the court remains open to alternatives or additions to its rent abatement formula.

A potential avenue for expanding tenant remedies presents itself when a landlord's actions in violation of the Residential Rental Agreements Act rise to the level of an unfair trade practice. In Borders v. Newton the court of ap-

130. See Note, supra note 114, at 1287-89.
131. Government income maintenance programs, such as rent subsidy programs and direct income redistribution programs, also enter into the broader housing policy milieu. See id. at 1289.
132. Surratt, 99 N.C. at 409, 393 S.E.2d at 561 (claim was for "rent abatement and ... not ... damages for breach of the covenant of habitability"); see supra text accompanying notes 39-40.
133. Surratt, 99 N.C. at 411, 393 S.E.2d at 562 (Greene, J., concurring in result) (rent abatement is a measure of damages for breach of implied warranty); see supra text accompanying notes 41-42.
134. Allen, 99 N.C. App. at 641, 394 S.E.2d at 482 (raising possibility that a tenant bringing action for breach of implied warranty "may also seek rent abatement"); see supra text accompanying notes 57-58.
137. 68 N.C. App. 768, 315 S.E.2d 731 (1984); see supra notes 111-12 and accompanying text.
peals left undisturbed a district court holding in support of such an action.\textsuperscript{138} Similarly, the \textit{Allen} court found that the tenant had presented evidence from which a jury could find an unfair trade practice.\textsuperscript{139} The court left unanswered, however, the question of which damages would be subject to the treble damages provision of section 75-16.\textsuperscript{140} The district court in \textit{Borders} trebled a security deposit as damages.\textsuperscript{141} Arguably, the court-ordered return of a security deposit is analogous to court-ordered rent abatement. This analogy would support the court trebling damages calculated by the \textit{Miller} rent abatement formula when a landlord’s violation of the Residential Rental Agreements Act rises to the level of an unfair trade practice. By allowing such an award, the court would penalize significantly those landlords who egregiously violate the Act.

The \textit{Surratt} and \textit{Allen} cases involved tenants who ceased paying rent and became defendants in summary eviction actions prior to vacating their rental units. The court held both times that the tenants’ withholding of rent did not preclude their recovery of damages for the landlords’ breaches of the implied warranty of habitability.\textsuperscript{142} Landlord Allen invoked the Act’s prohibition against unilateral rent withholding prior to judicial action,\textsuperscript{143} asserting that Simmons “waived her right to bring any action which arose out of her tenancy.”\textsuperscript{144} Professor Fillette has argued that such a broad interpretation of the prohibition would “largely negate” the Act’s section 42-41, which states that the obligations of the tenant and the landlord are mutually dependent.\textsuperscript{145}

The court of appeals qualified its statement of the recovery rights of the tenant who has withheld rent by noting that a tenant cannot collect rent abatement damages for a period when she did not pay rent.\textsuperscript{146} The court essentially defined rent abatement as a refund of rent; one obviously cannot get a refund of something one did not pay. This approach leaves unanswered, however, the question of the potential liability of the tenant who has withheld rent in response to his landlord’s breach. Judge Greene’s view that a tenant can assert the landlord’s violation of the implied warranty of habitability to seek an abatement of his overdue rent obligation\textsuperscript{147} is consistent with general law elsewhere.\textsuperscript{148} It would be incongruous to hold that a landlord’s attempt to collect rent for unfit

\textsuperscript{138} Borders, 68 N.C. App. at 770, 315 S.E.2d at 732.
\textsuperscript{139} Allen, 99 N.C. App. at 645, 394 S.E.2d at 484; see supra notes 59-64 and accompanying text.
\textsuperscript{140} See N.C. GEN. STAT. § 75-16 (1988) (providing for trebling of damages assessed for violation of unfair trade practice statutes).
\textsuperscript{141} Borders, 68 N.C. App. at 770, 315 S.E.2d at 731.
\textsuperscript{142} Allen, 99 N.C. App. at 642, 394 S.E.2d at 482; Surratt, 99 N.C. App. at 407, 393 S.E.2d at 560.
\textsuperscript{143} See N.C. GEN. STAT. § 42-44(c) (1984).
\textsuperscript{144} Plaintiff Appellee’s Brief at 7, Allen (No. 8921DC1155).
\textsuperscript{145} Fillette, \textit{supra} note 65, at 789; see N.C. GEN. STAT. § 42-41 (1984).
\textsuperscript{146} Allen, 99 N.C. App. at 642, 394 S.E.2d at 482; Surratt, 99 N.C. App. at 407, 393 S.E.2d at 560.
\textsuperscript{147} Surratt, 99 N.C. App. at 411, 393 S.E.2d at 562 (Greene, J., concurring in result); see \textit{supra} notes 41-42 and accompanying text.
housing could be an element of an unfair trade practice action, and yet hold a tenant who has withheld rent liable for more than the fair rental value of substandard housing.

If the tenant withholding rent without judicial approval is not thereby limiting his claim to damages, except for the obvious lack of a claim for a refund of rent, the prohibition on unilateral rent withholding must be, by process of elimination, applicable to the tenant's right to possession. One commentator has suggested that the unilateral withholding prohibition complements the requirement in section 42-25.6 that prohibits landlords from evicting tenants without resort to a judicial summary ejectment proceeding. Viewed from this perspective, the two provisions complement each other by denying either party possession rights if she attempts self-help remedies. North Carolina landlord and tenant law dealing with retaliatory eviction bars the retaliatory eviction defense to a summary ejectment claim when the tenant has failed to pay rent. This explicit linkage of the tenant's possession right and his duty to pay rent, in spite of possible wrongdoing by the landlord, lends further support to interpreting the unilateral withholding prohibition as creating a similar link.

Professor Fillette has argued for a narrower interpretation of the phrase "unilaterally withhold rent." He has suggested that, based on the mutuality of landlord and tenant obligations under section 42-41, a tenant's withholding of rent cannot be considered unilateral if the landlord previously breached the implied warranty of habitability. Professor Fillette also has stated that "[t]he terms 'wrongful' and 'unilateral' could be read synonymously in this context." This substitution of terms would essentially leave section 42-44(c) reading, "It is unlawful to withhold rent unlawfully." Thus, either by process of elimination or by following Professor Fillette's reasoning to its logical conclusion, section 42-44(c), if it has substantive content, denies rights of possession to the tenant who withholds rent before the landlord has been found by a court to have breached the implied warranty of habitability.

Although failing to clarify the unilateral rent withholding prohibition, the North Carolina Court of Appeals, in Surratt and Allen, has presented a formula for computing the contract damages of a tenant who has occupied unfit rental housing. The landlord is liable for the period of occupancy for which the court finds her to have breached the implied warranty of habitability under section 42-42(a). Damages are the lesser of the rental unit's fair rental value as warranted minus the fair rental value of the rental unit in its defective condition, and the agreed rent. The court has derived a reasonable measure of damages in applying a lease-based, agreed-rent ceiling to a "benefit of the bargain" measure.

149. Allen, 99 N.C. App. at 645, 394 S.E.2d at 484.
152. Fillette, supra note 65, at 790.
153. Id.
154. Id.
155. While the court also acknowledged the possibility of special and consequential damages, it did not discuss these types of damages.
of damages. The court was right to assert that withholding rent does not strip a tenant of the right to bring an action in breach of warranty against the landlord, but the court should have used the opportunity to clarify its interpretation of the statutory prohibition on unilateral withholding of rent.

The court of appeals has decided only four cases concerning contract damages for breach of the implied warranty of habitability in rental housing; none of these cases has reached the North Carolina Supreme Court. Future holdings should seek to reduce the remaining uncertainty concerning the legal obligations and potential liability of landlords and tenants. Holdings adhering to the three recommended principles that follow would add significantly to the certainty and equity of landlord and tenant law in North Carolina. First, the as-warranted fair rental value should be presumed equal to the agreed rent, if the tenant fails to prove that the premises were unfit when first occupied by the tenant. This approach would reduce both subjectivity and uncertainty of outcome in resolving valuation issues. Second, the courts should clarify the actions constituting unfair trade practices and the scope of damages to be trebled. Treble damages can be an appropriate and effective punitive remedy only if applied in a consistent manner to egregious circumstances. Third, the prohibition on unilateral rent withholding should have consequences only for the tenant’s right to possession of the premises.

The North Carolina courts have addressed the issue of contract damages for which a landlord is liable when in violation of the implied warranty of habitability. If future holdings adhere to the three principles presented above, landlords and tenants will operate in a more certain and predictable legal environment. This element of stability would be of particular value in the fragile market for low income housing.

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