6-1-1969

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sale of any security.” It seems unlikely that the court could have intended to weaken so substantially such a significant part of the Rule, but at least insofar as the civil remedy is concerned the effect of its language could have this result.

In denying the plaintiff the use of the Rule in this case, the court does not employ all the potential deterrent force it has available. All the court requires in order to bar a plaintiff from recovery under the Rule is that he believe that he is using some secret information. A different result in this case would have the effect of reducing the number of initial false statements, and recovery would not be dependent on the later actions of the one who received the information. The subsequent action by the plaintiff does not lessen the evil of giving false statements in the first place, and should not relieve the defendant of any liability, either civil or criminal. In short, the subjective intent of the tippee should not lessen the responsibility of an instigator who has clearly violated the Act himself.

ALEXANDER P. SANDS, III

Torts—Liability of Builder-Vendor’s Lender for Failure to Protect Vendee against Defective Home

In Connor v. Great Western Savings and Loan Association, the California Supreme Court held that a lender who provided financing for a subdeveloper had a duty to purchasers to exercise reasonable care to prevent the builder from constructing and selling defective houses. The subdeveloper was inexperienced and undercapitalized, and its lender retained substantial control over the subdevelopment planning almost to the point of being an entrepreneur without sharing attendant risks. Connor is a decision without precedent, and it pioneers a new area in a field that was already in a great state of flux—tort liability in the home-building in-

82 17 C.F.R. § 240.10b-5 (1968).
83 286 F. Supp. at 345.
1 — Cal. 2d —, 447 P.2d 609, 73 Cal. Rptr. 369 (1968) (Traynor, C.J., in a 4-3 decision).
2 The intermediate appellate court did reach almost the same result, however, in holding that Great Western owed purchasers of housing built by the subdeveloper a duty “at least to the extent of protecting these persons from gross structural hazards.” Connor v. Conejo Valley Dev. Co., 253 Cal. App. 2d —, —, 61 Cal. Rptr. 333, 344 (Dist. Ct. App. 1967).
Before the decision, California subscribed to the fast-developing majority view that builder-vendors are liable for their negligence to vendees and third parties who might foreseeably be injured by latent defects in home design and construction. But at least three jurisdictions have gone further and have held building contractors strictly liable in tort for the sale of defective homes.


State Stove Mfg. Co. v. Hodges, — Miss. —, 189 So. 2d 113, cert. denied, 386 U.S. 912 (1966) (Mississippi); Schipper v. Levitt & Sons, 44 N.J. 70, 207 A.2d 314 (1965) (New Jersey); Humber v. Morton, 426 S.W.2d 554 (Tex. 1968) (Texas). The Mississippi decision was based in part on the fact that a manufactured product—a water heater—caused the damage to the home. The court emphasized, however, that defendant contractors were held liable not only as retailers or wholesalers of the water heater but also as builders of the house in which it was installed. — Miss. at —, 189 So. 2d at 123. The New Jersey decision used some language that could be interpreted to mean a warranty liability rather than strict liability in tort. But in Rosenau v. City of New Brunswick, 51 N.J. 130, 238 A.2d 169 (1968), modifying 93 N.J. Super. 49, 224 A.2d 689 (Super. Ct. App. Div. 1966), the New Jersey Supreme Court emphasized that the statute of limitations and other sales warranty defenses are not applicable in tort suits against builder-vendors. Other jurisdictions have cited Schipper with approval or spoken of strict liability, but the fact situation and the language used implies more of a warranty liability theory than one of strict liability in tort. E.g., F & S Const. Co. v. Berube, 322 F.2d 782 (10th Cir. 1963); Bethalmy v. Bechtel, 91 Idaho 55, 415 P.2d 698 (1966); Jones v. Gatewood, 381 P.2d 158 (Okla. 1963); Waggoner v. Midwestern Dev. Co., — S.D. —, 154 N.W.2d 803 (1967); Haye v. Century Builders, 52 Wash. 2d 830, 329 P.2d 474 (1958).

After this case note went to press, Kriegler v. Eichler Homes, Inc., — Cal. App. 2d —, 74 Cal. Rptr. 749 (Dist. Ct. App. 1969) was handed down adding California to the jurisdictions that hold builder-vendors of defective homes strictly liable in tort for injuries to users of the homes and their property. Plaintiff homeowner brought an action for damages as a result of the failure of a heating system against the builder, a mass-producer of housing. Affirming a judgment in favor of the plaintiff, the court of appeal cited with approval Schipper v. Levitt & Sons, Inc., 44 N.J. 70, 207 A.2d 314 (1965). It observed that "in terms of today's society, there are no meaningful distinctions between Eichler's mass production and sale of homes and the mass production and sale of automobiles and . . . the pertinent overriding policy considerations are the same." — Cal. App. 2d at —, 74 Cal. Rptr. at 752. The court adopted the arguments made in Schipper that there is no real opportunity for the buyer effectively to inspect a house for defects and agreed that the builder-vendor is in the best position to bear the loss. Although the language of the court implies that strict tort liability for builder-vendors is
Connor could presage the application of strict liability to lenders who finance housing developers in those jurisdictions that hold builder-vendors strictly liable. This result would supplement favorably the policies behind holding builder-vendors liable for defective homes in cases where the lender retains a certain amount of control over the capital loaned. Arguably, the best policy result that will emerge from the disparity of liability law in the building field is that both builder-vendors, whether large or small, and their financial backers who retain any control over the project, whether one home or a subdevelopment, will be held strictly liable for any dangerously defective houses sold. With a substantial number of builder-vendors operating on such dangerously thin capitalization that plaintiffs with claims against them for defective homes may find it impossible to satisfy judgments,6 the home-construction industry is an area in which vicarious liability can be extended to lenders for valid social policy reasons.

Concededly, Connor involved liability of the lender predicated upon some fault—negligence—and the holding is revolutionary in extending the duty of the lender who backs a financially weak contractor to the vendees of the houses constructed. Since builder-vendors in California are liable to third-party users of homes for negligence in design and construction, it is reasonable to assume that Connor also imposes a duty on lenders that runs to such third parties. But the fact situation and the policy reasons set forth by the majority are also important in an argument for extending strict liability to lenders.

The situation in Connor was as follows: defendant Great Western Savings & Loan agreed to supply funds necessary for two contractors doing business as the Conejo Development Company to purchase a one-hundred acre tract and to construct homes thereon. Upon investigating the developer's financial condition, Great Western learned that it was extremely weak—the builder-vendor having only $5,000 capital when it started its development plans.7 Yet Great Western exercised less than normal care in making the loan and failed to examine the foundation plans, failed

limited to mass developers, these two basic arguments also can be applied to small builder-vendors of individual houses. See text p. 997 infra. Now that California has adopted strict tort liability for at least some classes of builder-vendors, the way has been cleared for holding their lenders strictly liable upon application of the criteria outlined p. 993 infra.

6 Comment, Liability of the Institutional Lender for Structural Defects in New Housing, supra note 3, at 740.

7 — Cal. 2d at —, 447 P.2d at 613, 73 Cal. Rptr. at 373.
to require soil tests, and failed "to discover gross structural defects that it could have discovered by reasonable inspection." Plaintiffs in two actions consolidated for trial were home-buyers who suffered serious property damage when foundations ill-designed for the adobe soil cracked.

Chief Justice Traynor, in reversing the trial court's nonsuit in favor of defendant Great Western, first concluded that the lender's acts of omission were sufficient for a finding of a negligent breach of duty to its shareholders, to whom it owed a duty not to finance defectively-built homes since the value of security for the construction loans depended on sound construction. But he also concluded that the lender was negligent in failing to take reasonable steps to prevent potential buyers from receiving defective homes and that it owed a duty of reasonable care to them.

Of great significance to the holding of a duty extending to the buying public was the finding that Great Western exercised significant control over the project. It dictated the price of the homes and insisted on substantial fees in excess of ordinary interest for making the construction loan to Conejo. It also received an agreement from Conejo to protect it from lost profits in the event that home-buyers could not be persuaded to obtain their loans through Great Western. Thus, concluded the majority of the court, the risk of harm foreseeable to the plaintiffs because of Conejo's "dangerously thin capitalization" was increased "by the additional pressures on Conejo ensuing from its onerous burdens as a borrower from Great Western."

Although California and most other jurisdictions have not yet accepted the theory of strict liability in tort for builder-vendors, Connor made

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9 Id. at —, 447 P.2d at 616, 73 Cal. Rptr. at 376.
10 Id.
11 Id. at —, 447 P.2d at 617-19, 73 Cal. Rptr. at 377-79. The policy reasons specifically set forth were that Great Western's transactions were intended to affect and did affect the plaintiffs to a significant degree; there was a foreseeable risk of harm to plaintiffs; the certain injury suffered by plaintiffs was closely connected with Great Western's negligent omissions; substantial moral blame attached to defendant; and the policy of tort law to prevent future harm called for extension of duty.
12 See note 5 supra. California has specifically refused to adopt the theory of strict liability in tort for builder-vendors. Conolley v. Bull, 258 Cal. App. 2d 749, 65 Cal. Rptr. 689 (Dist. Ct. App. 1968); Halliday v. Greene, 244 Cal. App. 2d 482, 53 Cal. Rptr. 267 (Dist. Ct. App. 1966). It is questionable, however, that the most important reason given for refusal—that a buyer of real property has an opportunity to inspect for defects—will withstand the language of the California Supreme Court in Connor. See text accompanying notes 17-18 infra. The other
most of the policy arguments that have been advanced for holding builder-
vendors strictly liable for selling defective homes. These arguments
generally have one underlying theory: the builder of a home should stand no
differently in the law than manufacturers of chattels who, in an increasing
number of jurisdictions,\footnote{See Prosser § 97, at 678-84.} are held strictly liable for defective products
unreasonably dangerous to persons or property.\footnote{Restatement (Second) of Torts § 402A (1965).}
The same arguments for holding both the manufacturer of chattels and the builder of homes
strictly liable follow quite logically. In Santor v. A & M Karagheusian, Inc.,\footnote{44 N.J. 52, 207 A.2d 305 (1965).}
a recent case involving a suit against the manufacturer of an
allegedly defective carpet, the New Jersey Supreme Court said,

> the great mass of the purchasing public has neither adequate knowledge
> nor sufficient opportunity to determine if articles bought or used are
defective. Obviously they must rely upon the skill, care and reputation of the maker. . . . [W]hen the manufacturer presents his goods to
> the public for sale he accompanies them with a representation that they
> holding manufacturers strictly liable in tort for personal injuries or property damage, but criticizes the result in Santor for allowing recovery for loss of bargain on
> the strict liability theory.}

Certainly the vast majority of the home-buying public also relies on the
skill, care and reputation of the builder. And if an ordinary citizen is
unable to tell whether carpeting, power tools, and the like are defective in
a manner dangerous to persons or property, he is usually less able to
detect defective conditions in the home he purchases. In Connor, Chief
Justice Traynor pointed out that “the usual buyer of a home, [sic] is ill-
equipped with experience or financial means to discern such structural

holding manufacturers strictly liable in tort for personal injuries or property damage, but criticizes the result in Santor for allowing recovery for loss of bargain on
the strict liability theory.}
defects. . . . Moreover a home is not only a major investment for the usual buyer but also the only shelter he has. Hence it becomes doubly important to protect him against structural defects . . . ."17

The theory often used in the past by courts unwilling to hold builder-vendors liable even for negligence in construction after a buyer accepted the house was that he had an opportunity to inspect the house and should have rejected it if defective.18 As a practical matter, however, it simply is not possible for the average home buyer to detect defects in the home that he is about to acquire; even an architect would generally be unable to discover a defective foundation.

Santor also based the strict liability of the manufacturer on the theory that it could best bear the expense of personal or property injuries sustained because of defects in a manufactured product, even if not caused by negligence of the defendant.19 This risk-spreading theory may be extended by logical analogy to builders of homes.20 They have the opportunity to insure or spread the risks through prices just as do manufacturers of chattels.

Chief Justice Traynor in Connor adopted the argument that prevention of future harm through the use of tort liability supported holding the lender liable to the home purchaser for negligence, for "[r]ules that tend to discourage misconduct are particularly appropriate when applied to an established industry."21 The risk of tort liability may not prevent injuries in many areas such as automobile driving, but an established industry with the habit of considering all of the angles of profit and loss is apt, as the court's language suggests, to take greater care to protect the public if it knows it could face damage suits for failure to check and control its activities.22 If strict tort liability is applied to builder-vendors and their financial backers, arguably they would exercise even more diligence to insure the safety of homes.

Courts, then, can rely on these basic reasons for the view that builder-vendors are strictly liable in tort: risk-spreading by the party most able to do so, the helplessness and disadvantage of the buyer, prevention of

18 See PROSSER § 99, at 694.
19 44 N.J. at 65, 207 A.2d at 311-12.
21 — Cal. 2d at —, 447 P.2d at 618, 73 Cal. Rptr. at 378.
22 This idea is also suggested in Brown, supra note 3, at 218.
future harm, and the general feeling that the party engaging in an enterprise for profit should bear the burden if something goes awry. *Connor* used the same reasons for holding that the lender had a duty extending to the home purchaser. It is arguable that California may reasonably adopt the policies underlying *Connor* to hold builder-vendors strictly liable. And with this foundation laid, California logically could go further and hold lenders in the situation of Great Western strictly liable for defects in houses sold by builder-vendors that they finance.

Such an ultimate extension can be supported by the language of the intermediate California appellate court in its treatment of *Connor*:23

Since we recognize the obligation of the manufacturer who has the capacity to launch numerous potentially hazardous products on the market, should we not be prepared to impose similar standards of responsibility on the experienced and knowledgeable home-lending institution when it financially launches an untried developer by assisting him to produce and sell residential units to the uninformed public?24

All of the policy arguments for holding manufacturers and builders strictly liable for defects in what they produce can be applied with equal force to savings and loan associations, banks, and other lenders who back the home-construction industry. The lender is familiar with the entire transaction and, in all practicality, is the moving force behind most housing developments today.25 Without the lender's money most builder-vendors could not carry out their projects. Because it controls the capital, the lender is in the best position to prevent fraud and defectively-designed or defectively-constructed housing.

Furthermore, lenders are better risk-bearers and risk-spreaders than are builders and subdevelopers. As the facts in *Connor* indicate, many of the builder-vendors in the residential construction field are undercapitalized and inexperienced; they are often insolvent or no longer in business by the time defects in their housing are discovered.26 Thus contractors who build and sell homes, even if held strictly liable for defects that prove dangerous, will often be too irresponsible or too insolvent to

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24 Id. at —, 61 Cal. Rptr. at 346.
26 Id. at 740.
have done anything, such as insuring, to spread the risks. Lenders, on the other hand, generally would tend to be more responsible and see that the risk is spread in at least two ways—by requiring the builder to insure or by charging the builder higher interest rates.27

Finally, extension of strict liability to lenders such as Great Western probably would enhance the possibility of preventing future harm from defective housing. Lenders logically would take greater precaution in approving development plans and in inspecting the progress of the construction if held strictly liable for unreasonably dangerous defects. This really would cast no greater burden upon them, for lending institutions already owe a duty of care to stockholders to make sure housing on which they loan money will be sound enough to serve as proper collateral. As standard practice, savings and loan associations normally check soil conditions for potential foundation hazards, usually at the borrower’s expense; inspect plans to insure that they are adapted to the building site; and check for structural defects during the course of construction when lending money for residential construction projects.28

Under the strict liability theory, lenders of course would not have to fear that they would be held accountable for any and all defects. The theory is founded upon the idea that the house will be reasonably fit for the purpose for which it is sold. Only if it is defective through a condition unreasonably dangerous to persons using it or to their property would strict liability be imposed.29

As illustrated by the fact situation in Connor, courts should consider a number of factors in determining whether to impose strict liability on a lender backing a builder-vendor. While the decisions necessarily must develop on a case by case basis, the experience of the builder-vendor, its solvency, the control exercised by the lending institution, and the degree to which the lender becomes enmeshed in the enterprise are all highly relevant elements for consideration concerning the ultimate issue of lender liability. For instance, a lender that so involves itself in the housing scheme that it in effect becomes an entrepreneur ought to bear the full risks of its involvement to the extent of strict liability. Lenders financing

27 For a discussion speculating as to the effect of these risk-spreading devices on the housing industry, see id. at 754-55.
28 United States Savings & Loan League, Construction Loan Procedures 5, 8, 36 (1966).
inexperienced or financially-weak builders should under the Connor doctrine exercise control over the projects to insure sound construction; but even if they choose not to do so, such lenders should be held strictly liable for housing defects since their money launched the homes on the market. On the other hand, lending institutions that provide money for experienced, solvent builders and that are not negligent toward potential purchasers for not exercising substantial control over the planning and construction of the homes, and that do not involve themselves in the enterprise to an extent greater than lending money outright to the builder-vendor should not face strict tort liability for defective homes. Indeed, under the holding in Connor, they would not be liable in negligence. The circumstances surrounding each case would determine, of course, the weight a court would give each relevant element.

One difficulty in holding lenders strictly liable may be the issue of whether the independent contractor who builds and sells one house at a time should be held strictly liable for dangerous defects. It has been suggested that courts may distinguish between the subdeveloper who builds a number of homes and the independent contractor. However, both Texas and Mississippi have declined to recognize any such distinction and the New Jersey Supreme Court did not take the opportunity to do so in a recent case. Logically lenders should not be held strictly liable where there is no basis for such liability in the builders that they support. But the decisions indicate that where courts are willing to apply strict liability to builder-vendors, the size of their operation makes no difference. Just as the large developer, the independent contractor

is in full control of the construction of the house and therefore is in the best position to assume the responsibility for remedying structural defects. If he reaps profits from his activities, he ought to bear the risks involved in these activities. Consequently, he will use greater care to protect the lives and property of users of the home.

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80 The basic argument in favor of such a distinction is that the small, independent contractor is a poor risk-bearer and risk-shifter. See, e.g., Note, Builder-Vendors: Liability for Negligence and for Breach of Implied Warranty of Habitability, 51 Cornell L. Rev. 389, 399-400 (1965); Note, 41 Wash. L. Rev. 166, 172-73 (1966); Recent Developments, the Strict Tort Liability of Builder-Vendors, 28 Ohio St. L.J. 343, 352 (1967).


83 Recent Developments, the Strict Tort Liability of Builder-Vendors, supra note 30, at 351 (citations omitted).
In short, the argument that the single contractor is often a poor risk-bearer and risk-shifter can be obviated if the lender who backs him is also held strictly liable.

Under any extension of strict liability to the lender, the builder-vendor should remain primarily liable since he is the one with the most immediate control over the construction. Then the lending agency can protect itself not only by spreading the risk through interest rates on loans and requiring the borrower to insure against products liability, but can also seek indemnification from a solvent builder who builds a defective house, at least if the builder was actively negligent. These methods of protection might make courts less reluctant in the future to extend the Connor principle so that lenders financing builder-vendors are strictly liable for housing defects.

When all arguments on the subject are examined, such vicarious strict liability for lenders must rest on a social policy concept rather than on a fault principle. But this is nothing new in the law of torts.

Vicarious liability is based on a relationship between the parties, irrespective of participation, either by act or omission, of the one vicariously liable, under which it has been determined as a matter of policy that one person should be liable for the act of the other. Its true basis is largely one of public or social policy under which it has been determined that, irrespective of fault, a party should be held to respond for the acts of another.

THOMAS F. LOFLIN III

Torts—Municipal Corporations—Liability for Failure to Provide Requested Police Protection Against Assault by a Third Person

The doctrine of immunity for municipal corporations has long been invoked to insulate municipalities from liability for the torts of their law enforcement officials. Even in those jurisdictions that have abolished

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34 See Comment, Liability of the Institutional Lender for Structural Defects in New Housing, supra note 3, at 760-61 & n.122.

1 On the doctrine of municipal immunity, see generally W. PROSSER, LAW OF TORTS 996-1013 (3rd ed. 1964) [hereinafter cited as PROSSER]. As to municipal liability for the torts of law enforcement officials, see 18 E. McQUEILLEN, MUNICIPAL CORPORATIONS §§ 53.79-53.81a (3rd ed. 1963); Comment, Municipal Liability for Police Torts: An Analysis of a Strand of American Legal History, 17 U. MIAMI L. REV. 475 (1963).