NOTE

LAST WALL STANDING: BUILDERS ARE FINDING A WAY AROUND THE HOUSING MERCHANT IMPLIED WARRANTY FOR NEW HOME CONSTRUCTION IN NEW YORK

I. INTRODUCTION

Imagine after years of saving, a young couple finally finds their dream home and makes the decision to buy it.[1] The home is everything they have ever imagined.[2] It is completely renovated with new electric and high-end appliances, new counters, new floors, and more.[3] They put in an offer on the house and quickly close on the property.[4] For the first few months, all goes well.[5] Then suddenly, their dreams become a nightmare as their home begins to literally fall apart beneath them.[6] They

1. Diana Olick, *Buyer Beware: Those Picture-Perfect Flipped Homes Can Be Masked Money Pits*, CNBC (Mar. 9, 2017, 2:28 PM), https://www.cnbc.com/2017/03/09/buyer-beware-those-picture-perfect-flipped-homes-can-be-masked-money-pits.html (explaining that Cameron McGuire and his wife thought they had found a move-in-ready dream home after deciding they wanted to downsize homes, only to discover six months later that the flipped home had both mechanical and structural issues).

2. *Id.*

3. *See* John Matarese, *Buying a Flipped Home? This Woman Has a Warning for You*, ABC ACTION NEWS (May 1, 2018, 11:07 AM), https://www.abcactionnews.com/money/consumer/dont-waste-your-money/buying-a-flipped-home-this-woman-has-a-warning-for-you (discussing that the developers spruced up the run-down home by installing new granite countertops, kitchen cabinets, and freshly painting all the walls, but did not pay any attention to the things that a buyer would not see, like the roof, wiring, plumbing, and foundation of the house).

4. Ilyce Glink, *Buying a Flipped House: Nightmare*, THINK GLINK (Jan. 20, 2020), https://www.thinkglink.com/2020/01/20/buying-a-flipped-house-nightmare (stating that the homebuyer found a newly flipped house that appeared to be "done to the nines[,]" and after an inspector could not find anything particularly concerning, she closed on the property only to find there were significant defects in the home that cost her around $20,000 to fix).

5. *See House Flipping Nightmares*, INSIDE EDITION (Feb. 9, 2015, 8:24 AM), https://www.insideedition.com/investigative/9681-house-flipping-nightmares.

6. *Id.* (explaining that after two weeks of living in her newly purchased flipped house, Maria Stapleton's garage door detached and the kitchen ceiling began to crack and cave in); *see also* Olick, *supra* note 1 (stating that six months after moving into a condo in a newly flipped house, the McGuires discovered that there were structural issues with the ceiling and many code violations and defects that would cost over $100,000 to repair).

realize that like many other unsuspecting buyers, they bought a "masked money pit" from a local developer-flipper who created the illusion of a dream home with some fresh paint.[7] Because buyers cannot "return a bad home," especially when the developer is nowhere to be found, these buyers are now stuck with the ever-growing expenses of a home that is dilapidated down to the foundation.[8]

Many people, at some point in their lives, will stand in the shoes of a buyer in a real estate transaction.[9] As a result, New York State has enacted legislation to protect the buyers of homes, specifically the buyers of newly constructed homes.[10] Buyers and sellers are not on equal footing in most real estate transactions with regard to their knowledge of the condition of the premises being transferred, especially when the seller is also the builder of the newly constructed home.[11] The builder is in a far better position than the seller to know about the condition of the premises and to discover defects.[12] "[I]nspection of realty is much more complicated than inspection of consumer goods," so many buyers must look to the help of experts.[13] Even if the buyer can afford to hire an expert examiner to inspect the premises for them, there are many issues within a home that an expert may miss.[14]

Unfortunately for many real property buyers, whether they purchase houses, condominiums ("condos"), or cooperative apartments ("co-ops"), it is only after they have settled into their home that they

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7. *See* Dannirose, *Almost Bought a Flipped House . . . What a Nightmare!*, HOUZZ, https://www.houzz.com/discussions/5493550/almost-bought-a-flipped-house-what-a-nightmare (last visited Aug. 1, 2021) (describing a buyer who almost bought a flipped home that was advertised as completely renovated, but backed out when she found out there were issues with the electrical systems, the sewer system, and the structure of the home); *see also* Matarese, *supra* note 3 (explaining that "masked money pits" are common when homes are flipped by amateurs who focus more on the aesthetic appearance of the home than they do on the structural and mechanical functioning of the home).

8. *House Flipping Nightmares*, *supra* note 5 (explaining that after discovering the defects in the flipped home, the developer would not return the buyers' phone calls); *see, e.g.*, Matarese, *supra* note 3.

9. McDonald v. Mianecki, 398 A.2d 1283, 1289 (N.J. 1979) (stating that "the purchase of a new home is not an everyday transaction for the average family"—on the contrary, "in many instances it is the most important transaction of a lifetime.").

10. *See* N.Y. GEN. BUS. LAW §§ 777–777-b (Consol. 1999).

11. DeRoche v. Dame, 430 N.Y.S.2d 390, 392 (N.Y. App. Div. 1980); Amy L. McDaniel, Note, *The New York Housing Merchant Warranty Statute: Analysis and Proposals*, 75 CORNELL L. REV. 754, 764 (1990) (stating that the parties to a housing sale contract "do not bargain as equals").

12. *See* McDaniel, *supra* note 11, at 763.

13. *Id.* at 773-74.

14. *Id.* at 774; *McDonald*, 398 A.2d at 1289; Barbara L. Dainoff, *Need Advice – I Bought a Bad Flip*, BIGGERPOCKETS, https://www.biggerpockets.com/forums/86/topics/567057-need-advice-i-bought-a-bad-flip (last visited Aug. 1, 2021) (explaining that even with an inspection, there are some defects that cannot be seen nor anticipated).

discover the shoddy workmanship and defective construction.[15] The popular image of house flippers comes from television, where a fun couple or a set of brothers takes a run-down, old house and completely revamps it.[16] Reality, as many inexperienced buyers learn the hard way, is quite different.[17] A flipped house is "a property purchased with the sole purpose of turning it around and selling it for a profit," so a flipper wants to complete these projects as fast as possible to minimize his own costs.[18] For many people who flip homes, this is their primary source of income—their business.[19] They have a "financial interest" in getting things done as quickly as possible, as they are looking to maximize their profits.[20] Many businessmen who are career flippers focus more on "putting lipstick on a pig" than taking the extra time to ensure the safety and satisfaction of their buyers.[21]

New York State had a common law version of the Housing Merchant Implied Warranty in place to protect buyers, but it was replaced with New York Consolidated Law Services General Business Law Article 36-B Section 777–777-b ("Article 36-B").[22] This statutory Housing Merchant Implied Warranty covers multi-unit residential buildings of five stories or fewer.[23] Although there is some contradicting legal precedent, custom homes, which are new homes built on

15. Matarese, *supra* note 3; Olick, *supra* note 1.

16. Caitlin Flanagan, *Beware the Open-Plan Kitchen*, VULTURE (Sept. 18, 2017), https://www.vulture.com/2017/09/the-ugliness-behind-hgtv-never-ending-fantasy-loop.html (explaining that Home & Garden Television is one of the most popular networks on television, and its multitude of house-flipping shows may be influencing viewers to try flipping houses themselves).

17. *See* Mark Ferguson, *How Realistic Are House Flipping Television Shows?*, INVESTFOURMORE (Mar. 4, 2020), https://investfourmore.com/how-realistic-are-house-flipping-television-shows (describing that house-flipping television shows are not only inaccurate, but also set bad examples for inexperienced people watching the show who may be considering attempting to flip houses); Ethan Roberts, *Home Flipping: The Reality (What TV Doesn't Tell You)*, AUCTION (May 24, 2019), https://www.auction.com/blog/home-flipping-the-reality-what-tv-doesnt-tell-you.

18. Ben Hendricks, *Your New Flipped House Will Be a Disaster . . . Probably*, ABI HOMES, https://abihomeservices.com/home-inspection-finds-flipped-houses (last visited Aug. 1, 2021) (explaining that "the longer the home sits the more money the flipper loses").

19. Roberts, *supra* note 17 (describing an experienced investor who states that flipping homes can be "a fun and rewarding way to generate income").

20. Hendricks, *supra* note 18; Ferguson, *supra* note 17.

21. Hendricks, *supra* note 18 (describing two ways that flippers will focus on the "bling factor" because "kitchens and bathrooms sell houses," and they will assure you that everything has been replaced, so you will not find anything in inspections); Olick, *supra* note 1.

22. Anthony W. Cummings, *"*Caceci *is Dead, Long Live* Caceci*": Article 36-B Warranties on the Sale of New Homes*, 4 HOFSTRA PROP. L.J. 47, 51 & n.21 (1990).

23. *See* N.Y. GEN. BUS. LAW § 777 (Consol. 1999). An implied warranty is an assurance by the seller that is guaranteed irrespective of whether the seller has expressly promised it orally or in writing. The Audiopedia, *What Is Implied Warranty? What Does Implied Warranty Mean? Implied Warranty Meaning*, YOUTUBE (Oct. 3, 2016), https://www.youtube.com/watch?v=l58n1nCFSIU.

previously owned land, do not fall within the definition of a "new home."[24] It also does not include condos and co-ops that are located in buildings of six or more stories, which are very common in New York City.[25] The statute does not define the difference between a newly constructed home and a renovated home, nor does it say how much of a home must be left physically standing after a flip for it to fall outside of "new" construction.[26] As a result of this gap in the statute, some builders will leave an insignificant part of the existing premises standing, such as one singular wall of the garage, and claim that the house is renovated and not "new," so that they can withhold from buyers the six-year warranties guaranteed by the New York statute.[27]

Amending Article 36-B to clearly define "new home construction" and create a bright-line rule that professional developers must follow will greatly increase protections for buyers.[28] Flipping houses has become a popular source of income for many people, so this amendment would be tailored to ensure that the buyers of newly reconstructed homes, who are at a higher risk for physical, as well as economic, harm, get the protections that the New York Legislature intended for them to have.[29] In addition, if the protections under Article 36-B were expanded to include coverage to purchasers of condos or co-ops in buildings with six or more stories, buyers in heavily populated urban areas would be better protected.[30]

The purpose of this Note is to suggest a way to better achieve the legislative purpose behind this relatively new statute and to help protect the unknowingly disadvantaged buyer, a party whom society has a great interest in protecting.[31] This Note will begin in Part II by discussing the

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24. Watt v. Irish, 708 N.Y.S.2d 264, 266-67 (Sup. Ct. 2000) (holding that custom homes are not included in the definition of "new home"); Thomas S. Tripodianos, *Statutory Warranty*, WB&G ATT'YS AT L. (May 2007), https://www.wbgllp.com/single-publication.php?type=1&id=64. *But see* Gorsky v. Triou's Custom Homes, Inc., 755 N.Y.S.2d 197, 208 (Sup. Ct. 2002) (holding that custom homes are protected by the statutory warranty).

25. GEN. BUS. §§ 777–777-b; Bd. of Managers of Beacon Tower Condo. v. 85 Adams St., LLC, 25 N.Y.S.3d 233, 236, 238 (App. Div. 2016).

26. *See* GEN. BUS. §§ 777–777-b.

27. Cummings, *supra* note 22, at 58 (stating that the drafting of the statute will allow builder-vendors to look for loopholes); GEN. BUS. § 777-a.

28. *See* GEN. BUS. §§ 777–777-b.

29. Caceci v. Di Canio Constr. Corp., 526 N.E.2d 266, 269 (N.Y. 1988) (discussing the distinction between a contract for the sale of a completed home and a contract for the sale of a new home). When contracting for the sale of a new home, inspection of the home is oftentimes an impossibility, as the home may not be fully constructed or as a result of the nature of latent defects. *Id.* at 59.

30. *See* GEN. BUS. §§ 777–777-b.

31. Lynn Y. McKernan, Note, *Strict Liability Against Homebuilders for Material Latent Defects: It's Time, Arizona*, 38 ARIZ. L. REV. 373, 373, 388 (1996) (stating that the purchase of a

history of real estate transactions and the principle of caveat emptor.[32] It will then discuss the policy reasons behind the shift to the common law "Housing Merchant" doctrine.[33] In Part III, this Note will concentrate on New York's statutory Housing Merchant Implied Warranty and its replacement of the common law.[34] It will then go on to analyze the protections that buyers of new home construction receive in different states, as compared to buyers in New York.[35] Part IV will propose an amendment to Article 36-B, which will specifically include a provision governing professional investors who "flip" houses.[36] Lastly, Part V will conclude this Note and reiterate the ways in which an amendment to the New York law can further protect buyers of new home construction.[37]

II. THE SHIFT FROM CAVEAT EMPTOR TO THE COMMON LAW HOUSING MERCHANT DOCTRINE

This Part will describe the history of protections for buyers of real estate before the New York Legislature enacted a statutory warranty.[38] Subpart A will discuss caveat emptor and how real estate transactions have applied it throughout history.[39] Subpart B will address how changes in the types of buyers, sellers, and home defects have caused caveat emptor to lose its usefulness.[40] Finally, Subpart C will address the protections and applications that existed under the common law Housing Merchant Doctrine.[41]

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home is very likely the most important and costly acquisition that the average consumer will ever make).

32. *See infra* Part II.B; *see, e.g.*, McDonald v. Mianecki, 398 A.2d 1283, 1289 (N.J. 1979).

33. *See infra* Part II.B; *Caceci*, 526 N.E.2d at 267-68.

34. *See infra* Part III; GEN. BUS. §§ 777–777-b.

35. *See infra* Part III.D; Alisa Marie French, *Florida's Implied Warranty of Habitability: How Far Does a Homebuyer's Protection from a Developer's Ticky Tacky Construction Extend?*, 44 STETSON L. REV. 925, 945-47 (2015).

36. *See infra* Part IV; GEN. BUS. §§ 777–777-b; Lylla Younes, *NYC House Flipping Is on the Rise, Exacerbating Gentrification*, GOTHAMIST (May 31, 2018, 7:28 AM), https://gothamist.com/news/nyc-house-flipping-is-on-the-rise-exacerbating-gentrification (explaining that "flipping a home involves buying and selling it within one year of purchase.").

37. *See infra* Part V; *Caceci*, 526 N.E.2d at 269.

38. *See infra* Part II; Fumarelli v. Marsam Dev., Inc., 703 N.E.2d 251, 253 (N.Y. 1998) (describing that before the statutory warranty existed, there was a common-law warranty for buyers).

39. *See infra* Part II.A; *see, e.g.*, Alex M. Johnson, Jr., *An Economic Analysis of the Duty to Disclose Information: Lessons Learned from the Caveat Emptor Doctrine*, 45 SAN DIEGO L. REV. 79, 101-02 (2008) (explaining that caveat emptor first emerged in ancient Rome and was only later embraced in real estate transactions in sixteenth-century England).

40. *See infra* Part II.B; McKernan, *supra* note 31, at 373, 388.

41. *See infra* Part II.C; *Caceci*, 526 N.E.2d at 267.

A. History of Caveat Emptor

Caveat emptor[42] is a Latin phrase which means "let the buyer beware."[43] In the legal sphere, it was a doctrine that traditionally governed the sale of personal and real property and emphasized that a buyer buys at his or her own risk.[44] Although this doctrine is often associated with sixteenth-century England, its origins actually trace back to ancient Rome.[45] England first applied the doctrine in the sale of chattels,[46] but by the early seventeenth century, it was adopted as a part of English common law and applied to both real and personal property.[47] By the nineteenth century, caveat emptor became a "central governing principle of land conveyancing law" in the United States.[48] It was applied even more universally in the United States than it was in England, and it was accepted by nearly all the states.[49]

This doctrine grew out of the nineteenth-century political and economic philosophy of laissez-faire, which asserted that a "buyer deserved whatever he got" if he was relying only on his own inspection.[50] During this period, judges looked at the purchase of land as "a game of chance."[51] In addition, caveat emptor served a gate-keeping function for the judicial system at a time when the courts here were beginning to take shape as an "effective organ for dispute resolution."[52]

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42. Frederick C. Wamhoff, *Property – Caveat Emptor – Duty to Disclose Limited to Commercial Vendors.* Ollerman v. O'Rourke Co., *94 Wis. 2d 17, 288 N.W.2d 95 (1980) and* Kanack v. Kremski, *96 Wis. 2d 426, 291 N.W.2d 864 (1980)*, 64 MARQ. L. REV. 547, 548 (1981). The entire expression is "*Caveat emptor, qui ignorare non debuit quod jus alienum emit*," which means "let a purchaser, who ought not be ignorant of the amount and nature of the interest, which he is about to buy, exercise proper caution." *Id.* (emphasis in original).

43. *Caveat Emptor*, BLACK'S LAW DICTIONARY (11th ed. 2019).

44. *Id.*; *Caceci*, 526 N.E.2d at 267-68.

45. Johnson, *supra* note 39, at 101-02; Alan M. Weinberger, *Let the Buyer Be Well Informed? – Doubting the Demise of Caveat Emptor*, 55 MD. L. REV. 387, 391 & n.30 (1996) (explaining that an exception to the Roman doctrine of caveat emptor required disclosures by sellers with regard to slaves, cattle, horses, and other drought animals, unless the flaws were so obvious that an ordinary buyer would notice them or the flaw was not serious enough to interfere with the usefulness of the slave or animal).

46. Weinberger, *supra* note 45, at 391 & n.29 (discussing that caveat emptor was mentioned in a text published in 1534 containing advice on horse trading: "[I]f he be tame and have been rydden upon, then *caveat emptor*.") (emphasis in original).

47. *See id.* at 391-93.

48. *See, e.g.*, *id.* at 393.

49. *Id.* at 393 & n.50 (explaining that the courts in all the States of the Union, except South Carolina, accepted caveat emptor).

50. McDonald v. Mianecki, 398 A.2d 1283, 1287 (N.J. 1979).

51. *Id.*

52. Weinberger, *supra* note 45, at 393-94 (explaining that the influx of claims from disappointed purchasers would overburden the judicial system). *But see* Johnson, *supra* note 39, at 89 (arguing that the "cheapest cost avoider" would be the seller's disclosure concerning the quality

Although an occasional injustice under this doctrine was expected, theorists argued that this was a reasonable trade-off in order to protect and promote an independent judiciary.[53]

Caveat emptor rested on two well-accepted assumptions.[54] First, that each party to a real estate transaction had equal access to information about the quality of the property and, therefore, equal bargaining power.[55] Second, that manufacturers and sellers of property were not in the business of supplying information, only the actual product, so the failure to supply information to buyers should not have been a legal basis for liability.[56] Under this doctrine, a buyer was expected to inspect the good carefully, at his or her own risk, and if the inspection revealed a defect or issue, the purchaser could take it upon him or herself to renegotiate.[57] If the purchaser was not confident in his or her ability to inspect, he or she could try to get an express warranty.[58] The seller had no obligation to disclose facts of which the buyer was unaware, regardless of their impact on the value of the property being sold.[59] In application, caveat emptor barred remedies against builders, except as covered by express warranties or representations, leaving many buyers to shoulder the cost of shoddy workmanship.[60]

Caveat emptor provided a "safe harbor" for sellers looking to avoid being sued for misrepresentation, but, unfortunately, the sellers' benefit was at the expense of the buyer.[61] "Silence was golden" for the seller,

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of the dwelling and any potential defects, unless the seller "made a deliberate investment in acquiring his knowledge which he would not have made had he known he would be required to disclose to purchasers").

53. *See* Weinberger, *supra* note 45, at 393-94 (suggesting that, eventually, cases of individual injustice as a result of caveat emptor would decrease as buyers became familiar with the doctrine of caveat emptor and how it was applied to the marketplace for both real and personal property).

54. *See* Weinberger, *supra* note 45, at 390-91; *cf.* Johnson, *supra* note 39, at 116 (explaining that caveat emptor relies on two assumptions: (1) "the premises being conveyed are simple and easy to inspect"; and (2) "each party to the transaction has equal access to information regarding the quality of the premises").

55. *See* Johnson, *supra* note 39, at 116; *see also* Weinberger, *supra* note 45, at 390-91.

56. *See* Weinberger, *supra* note 45, at 391.

57. *Caveat Emptor (Buyer Beware)*, CFI, https://corporatefinanceinstitute.com/resources/knowledge/other/caveat-emptor-buyer-beware (last visited Aug. 1, 2021); Johnson, *supra* note 39, at 102.

58. *See* Johnson, *supra* note 39, at 102-03 (explaining that the seller was not liable for any defects in the property that were either latent or patent); McDaniel, *supra* note 11, at 764; *see also Caveat Emptor (Buyer Beware)*, *supra* note 57 (stating that the buyer must do the necessary due diligence before a purchase to ensure the purchase suits his or her needs).

59. *See, e.g.*, Johnson, *supra* note 39, at 102.

60. *See* Cummings, *supra* note 22, at 51.

61. Johnson, *supra* note 39, at 104. Caveat emptor was a way for sellers to shield themselves from an action brought against them under intentional misrepresentation or fraud, or negligent misrepresentation or "innocent" misrepresentation. *Id.* at 103.

who had no duty to warrant the condition and quality of the premises.[62] The harsh and inequitable results of caveat emptor in the context of the sale of real property were obvious, especially when compared to the protections a consumer received when purchasing personal goods.[63] The system under caveat emptor afforded "greater protection to the purchaser of a seventy-nine cent dog leash than it [did] to the purchaser of a 40,000-dollar house," because the sale of personal property guaranteed the buyer an implied warranty of merchantability or fitness for a particular purpose, but the sale of real property did not.[64]

B. Shift in Real Estate Practices

This Subpart will break down three different changes in the real estate market: the seller, the buyer, and the defects.[65] It will briefly address the historical background and traditional role of each party in the sale of property.[66] It will then describe how caveat emptor in residential property transactions was displaced as a result of cultural shifts following World War II.[67]

1. Change in the Seller

After World War II, home-buying practices and home buyers started changing quickly.[68] With the economic growth of the post-war years, middle class people began to move more often, which caused a shift to a more "accelerated" construction.[69] The building industry underwent tremendous changes from artisans selling specially designed homes to builders mass producing homes overnight.[70] Home

62. *Id.* at 102.

63. Wamhoff, *supra* note 42, at 548.

64. *See* McDonald v. Mianecki, 398 A.2d 1283, 1288 (N.J. 1979). *But see* Wamhoff, *supra* note 42, at 559 (arguing that extinguishing caveat emptor expands the legal duties of sellers so far that it will create a "rash of litigation").

65. *See infra* Part II.B; Johnson, *supra* note 39, at 117-18.

66. *See infra* Part II.B.1–3; Weinberger, *supra* note 45, at 392-93.

67. *See infra* Part II.B.1–3; McKernan, *supra* note 31, at 373.

68. McKernan, *supra* note 31, at 373; Weinberger, *supra* note 45, at 395.

69. *See* McKernan, *supra* note 31, at 373; Weinberger, *supra* note 45, at 395; Johnson, *supra* note 39, at 118.

70. *See* McDonald v. Mianecki, 398 A.2d 1283, 1287 (N.J. 1979); *see also* Nancy B. Burlingame, *New York State Warranties on Sales of New Homes Act: From Caveat Emptor to Statutory Warranty Protection*, 4 ST. JOHN'S J. LEGAL COMMENT. 291, 292 (1989). *But see* Johnson, *supra* note 39, at 117-18 (arguing that formerly in the Middle Ages, structures were largely indistinguishable from each other, whereas now, a "comparison of one hundred dwellings in a community chosen at random would reveal one hundred different homes when measured by size, design, features, [and] complexity," which is where the inequality in knowledge comes from, as buyers are less likely to be able to become an expert with respect to a dwelling they are looking to

construction shifted to an "assembly line" process, where buyers no longer had the same intimate oversight over the building stages and development that so many had before.[71] Sellers no longer focused on building the home to meet the individual buyers' expectations; rather, builders were now looking to sell a "package deal" of a pre-constructed home and a plot of land.[72]

Like buyers, sellers too became less knowledgeable about property and home construction.[73] Nonetheless, sellers maintained their superior bargaining power over buyers because they were more familiar with the property itself.[74] In recent years, many developer-sellers know even less about construction and building maintenance as the trend of flipping houses has enticed many untrained and inexperienced people to take on massive home renovation projects.[75] Typically, only after these amateur developers have begun the project and sunk considerable money into it, do they realize that they are in over their heads.[76] For every month that the developers hold onto the property, they have to pay home insurance, property taxes, and utilities on top of all the other items in their construction budget.[77] As more unscheduled time passes, as it often

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buy). Today, homeowners and builders often interpret uniqueness and individuality as indicative of the value of a home. *Id.* As uniqueness of homes increase, a buyer's knowledge decreases, making them less able to make a "meaningful inspection." *Id.*

71. James Cotton, Note, *Are New Jersey Lawmakers Taking Maxwell's Silver Hammer Away from Homebuilders? Assessing the Effectiveness of the Upcoming Amendments to the New Jersey New Home Warranty and Builders' Registration Act*, 33 SETON HALL LEGIS. J. 259, 264-65 (2008); McKernan, *supra* note 31, at 373.

72. *McDonald*, 398 A.2d at 1287. "To apply the rule of caveat emptor to an inexperienced buyer, and in favor of a builder who is daily engaged in the business of building and selling houses is manifestly a denial of justice." McKernan, *supra* note 31, at 373-74 & n.9 (quoting Bethlahmy v. Bechtel, 415 P.2d 698, 710 (Idaho 1966)).

73. Johnson, *supra* note 39, at 118.

74. *Id.* at 95-96. Both vendors and buyers were no longer "jack[s]-of-all-trades," so in that sense, there was equality of bargaining power. *Id.* at 118. The inequality stemmed from the fact that sellers were able to occupy the premises, whereas buyers only had "episodic" access to the premises and by existing on the premises, they would inherently acquire knowledge with regard to the condition of the premises. *Id.* at 95-96.

75. S.L. Brown, *Dismantling My Dreams, One Brick at a Time*, SLATE (Dec. 24, 2018, 11:04 AM), https://slate.com/human-interest/2018/12/real-estate-house-flipping-renovation.html (describing a couple who were both practicing lawyers with no experience in building or developing property, but always had a dream of flipping a house so they could "escape the office"); Flanagan, *supra* note 16.

76. Brown, *supra* note 75 (explaining how a set of inexperienced, first-time flippers dipped into their savings with the reliance that they would recoup their investment, only to find that their experience was very different from what they had seen on television).

77. Jon Gorey, *4 Big Things to Consider Before You Buy a Flipped House*, APARTMENT THERAPY (Aug. 8, 2018), https://www.apartmenttherapy.com/flipped-houses-pros-cons-260140 (explaining that these costs incentivize flippers to cut corners on safety and quality in order to rush the completion of the project).

does, these flippers' sole objective is to get the house off their hands as quickly as possible, which is the perfect recipe for a flipped house gone wrong.[78]

2. Change in the Buyer

At the height of caveat emptor, the marketplace was based primarily on face-to-face interactions where local trade was "an arm's length proposition with wits matched against skill."[79] Buyers of goods in these agrarian societies were more hands on and would often inspect goods by both "look and feel."[80] The same was true of sales interactions in real property: buyers of real property often knew the sellers well.[81] Buyers were accustomed to haggle at length with vendors over price, as they "were more likely to feel ashamed of being outsmarted than angry at having been cheated."[82]

The courts recognized that as society changed, industrial-age purchasers became less "handy" than their ancestors and were simply "ill equipped" to effectively inspect property.[83] Many purchasers were "inexperienced" and "unsophisticated," which put them at a considerable disadvantage to the sellers who were far more familiar with the property.[84] Buyers became susceptible to the empty promises sellers made before their purchase was final, as they had no other choice than to rely on the skill and experience of those builders.[85]

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78. Danny Johnson, *Here's Why Everybody Keeps Failing at House Flipping*, BUS. INSIDER (Oct. 18, 2012, 5:44 PM), https://www.businessinsider.com/why-people-fail-at-house-flipping-2012-10 (stating that "doing a deal to just do a deal can quickly result in disaster"); Brown, *supra* note 75.

79. Weinberger, *supra* note 45, at 392 & n.34 (quoting Allison Dunham, *Vendor's Obligation as to Fitness of Land for a Particular Purpose*, 37 MINN. L. REV. 108, 110 (1953)). The "case of *Chandelor v. Lopus* is often regarded as the origin of caveat emptor under English common law[,]" and demonstrates the value placed upon a purchaser's wit. *Id.* at 392-93. Here, the court found that even though a jeweler told his customer that a jewel was a particular type of rare stone before selling it to him, this was not a warranty of the seller, and the buyer was responsible for determining if the jewel was in fact a "bezar stone" before purchasing the stone. *Id.*

80. *Id.* at 392.

81. *Id.*

82. *Id.* at 392-93 (explaining that English courts that applied caveat emptor were not interested in "enforcing the fairness of an exchange[,]" as they thought the contracting parties should be responsible for that).

83. *See* Johnson, *supra* note 39, at 100-01 (describing the new-age buyer who has evolved so far from the farmer of the Middle Ages that they can no longer even change a light bulb); *see also* Daniel J. Losito, Note, *New York's Implied Merchant Warranty for the Sale of New Homes: A Reasonable Extension to Reach Initial Owners?*, 91 COLUM. BUS. L. REV. 373, 375 (1990).

84. *See* McKernan, *supra* note 31, at 373.

85. DeRoche v. Dame, 430 N.Y.S.2d 390, 392 (N.Y. App. Div. 1980) (stating that the builder has all the knowledge with regard to the quality of materials used, quality of workmanship, and process of construction used in the completion of the project); Losito, *supra* note 83, at 375.

3. Change in Defects

Caveat emptor made sense in the nineteenth century, when common practice was to buy a plot of land and then hire an architect to build a home according to the agreed-upon plan.[86] The buyers were able to proactively watch over the progress of the builder because they paid the builder in stages, so they would become aware of any issues with the construction of their new home as they arose.[87] In addition, the structures were so basic and simple that defects were "patent"[88] and easily discoverable to the buyer.[89] The "equal access principle" applied in this context, as structures typically consisted of four walls, a dirt floor, and a simplistic thatched roof.[90] Regardless of how long the seller had owned the premises, it was assumed that the seller did not have any information that was not easily accessible to the buyer given how rudimentary most structures were at the time.[91] During this period, it was reasonable for buyers to assume that "what you see is what you get."[92]

Eventually, as technology advanced and architecture became more complex, "patent defects became latent[93] defects."[94] With the universal integration of complex plumbing, heating, air, and ventilation systems into modern structures, it became harder for the buyer to see defects as they were often hidden in the walls.[95] Even with proper inspections,

86. *See* McDonald v. Mianecki, 398 A.2d 1283, 1287 (N.J. 1979); *see also* Cotton, *supra* note 71, at 264-65.

87. *See McDonald*, 398 A.2d at 1287.

88. *Patent*, BLACK'S LAW DICTIONARY (11th ed. 2019). "Patent" is defined as obvious or apparent. *Id.*

89. Johnson, *supra* note 39, at 98 (explaining that the obvious nature of defects is what extinguishes the need for communication about the defects).

90. *See id*. at 116 (discussing how modern structures do not resemble dwellings from the time that caveat emptor was being developed—the structures from the Middle Ages were about four times smaller, did not have windows, and the door was a basic wooden door).

91. *Id.*

92. *Id.*; *The Meaning and Origin of the Expression: What You See Is What You Get*, PHRASE FINDER, https://www.phrases.org.uk/meanings/what-you-see-is-what-you-get.html (last visited Aug. 1, 2021) (stating that "what you see is what you get" was a phrase that often indicated a form of no-fuss trading).

93. *Latent*, BLACK'S LAW DICTIONARY (11th ed. 2019). "Latent" is defined as concealed or dormant. *Id.*

94. Johnson, *supra* note 39, at 98, 120. As structures became less simple, a homeowner's casually acquired knowledge with regard to the condition of the premises became vaster and more unique. *Id.*

95. *Id.* at 116; Olick, *supra* note 1 (explaining that after their purchase, a new inspector walked through their home, and "it was as if demons suddenly seeped out of the walls").

defects often go unnoticed.[96] The most dangerous and costly defects in a home are very often the ones that are the hardest to see.[97]

C. Implications of a Common Law Housing Merchant Doctrine

This Subpart will address overturning the precedent of caveat emptor.[98] It will then discuss the introduction and application of New York's common law Housing Merchant Doctrine.[99] Finally, it will examine what currently remains of caveat emptor in the real estate market.[100]

1. Application of Common Law Doctrine

New York State, along with many other states, was hesitant to recognize an implied warranty of habitability and workmanlike construction in new homes.[101] In 1967, the New York State Legislature's Law Revision Commission authorized a study, and the Commissioner supported the passage of two Bills that would place liability on "housing merchants."[102] These Bills never made it past the Judiciary Committee in the Senate and the Mortgage Committee in the Assembly, however.[103]

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96. *See* Dainoff, *supra* note 14; *see also* Glink, *supra* note 4 (explaining that inspectors have begun to rely more and more on checklists and often defects are missed, as they only go down the list of items and do not actually take time to note the condition of the property).

97. Johnson, *supra* note 39, at 97 n.45 (explaining that once latent defects became common, the displacement of caveat emptor was logical from an economic standpoint, because it was cheaper to have a seller disclose casually acquired information—information that he did not have to make a deliberate investment to discover—and that it would be the buyer who would incur the cost of a repair for a latent defect); Dainoff, *supra* note 14 (describing a buyer who purchased a flipped home that is now unsafe and unlivable); Matarese, *supra* note 3 (stating that latent defects in a newly purchased flipped home will cost the buyer around $12,000).

98. *See infra* Part II.C; Caceci v. Di Canio Constr. Corp., 526 N.E.2d 266, 267-68 (N.Y. 1988).

99. *See infra* Part II.C.1.

100. *See infra* Part II.C.2; *Caceci*, 526 N.E.2d at 267-68, 269.

101. *See* Burlingame, *supra* note 70, at 295.

102. *Id.* at 295 & n.15 (stating that Professor Ernest F. Roberts, Jr. examined the trends of consumer protections towards homeowners in the United States and found that, particularly in New York, the courts were "ambivalent towards utilizing implied warranties on homes under construction, much less newly built homes."). The study concluded that a mass developer of a house was very much like a manufacturer, and, therefore, new home construction should fall within the warranties covered by Article 2 of the Uniform Commercial Code ("UCC"). *Id.* at 295 n.16. The study equated new homes to goods and suggested the same attention and protections should be extended to the housing market. *Id.* The Commissioner also suggested that a housing merchant should be required to provide a bond to the purchaser just in case the merchant refused to later satisfy his liability. *Id.* at 296 n.16.

103. *Id.* at 295, 296 n.17 (explaining that the Bill that failed to be enacted would have placed liability on merchants for personal injuries and breach of warranties).

In light of the continued change in the practice of home purchases and the continued inaction of the legislature, New York courts began to move away from caveat emptor and imply a "warranty of the habitability or workmanlike construction" in real estate purchases for new homes.[104] Caveat emptor no longer applied in purchases of newly constructed homes, courts started holding in the 1980s, because it was in accord with principles of public policy to expect that structures be constructed in a skillful manner free from material defects.[105] Even without an express promise, the courts held that it was reasonable for purchasers to expect that the house they had purchased would be habitable.[106]

In *Caceci v. Di Canio Construction Corporation*,[107] the New York Court of Appeals created an implied warranty whose scope was limited to include only purchasers that had direct privity with the builder-vendor for the contract of a sale of a home.[108] This warranty also extended to the purchasers of condos and co-ops.[109] Similar to the application of the Uniform Commercial Code ("UCC"), this implied warranty did not require the seller to "deliver higher quality goods," just to deliver the "medium quality" home that a buyer is reasonably relying on the seller to produce.[110] New York courts also clarified that a home was still considered new construction, even if the house was recently completed by the builder before the purchaser bought it.[111] Under the common law, the court in *DeRoche v. Dame*[112] defined a new home as a house that had been "unoccupied," but with one blurry caveat that worked in the

104. *See Caceci*, 526 N.E. at 269, 270 (explaining that the courts were not compelled to wait for the legislature to act if there was a clear answer at hand). Precedent was not intended to create rigidity, but to assure certain and stable justice. *Id.* at 59. Therefore, if justice was not being achieved by adhering to precedent and such precedent was only creating confusion, then the courts have a right to overrule precedent and apply a rule that satisfies modern-day needs. *Id.* at 59-60.

105. *See* DeRoche v. Dame, 430 N.Y.S.2d 390, 392 (N.Y. App. Div. 1980); *see also Caceci*, 526 N.E.2d at 269 (stating that the builder-vendor was the only one who could prevent the occurrence of major defects, so it was fair to place the burden of loss on that party).

106. *DeRoche*, 430 N.Y.S.2d at 392 (explaining that, often times, a contract will be written in terms of the sale of realty, but really buyers see the transaction primarily as the "the purchase of a house, with the land incident thereto"); *see also Caceci*, 526 N.E.2d at 269-70 (explaining that caveat emptor placed an unfair burden on purchasers).

107. 526 N.E.2d 266.

108. *Id.* at 267, 270.

109. *See* Fumarelli v. Marsam Dev., Inc., 703 N.E.2d 251, 252-53 (N.Y. 1998) (describing the plaintiff who was arguing that the statute was not a complete substitute for the common-law remedy because under the common-law remedy, they would have a claim against the developer of their luxury condominium).

110. McDaniel, *supra* note 11, at 760-61 & n.46 (explaining that implied warranties "give[] effect to the parties' unarticulated contractual agreements about quality, and respond[] to the common perceptions of fairness and justice").

111. *See DeRoche*, 430 N.Y.S.2d at 392.

112. 430 N.Y.S.2d 390.

buyer's favor.[113] It stated that "limited occupancy" would not defeat the warranty, so, for example, if a builder lived in the house for a short time before selling it, this "limited occupancy" by the builder-vendor did not deprive the buyer of coverage of the implied warranty of workmanlike construction and habitability.[114]

2. Caveat Emptor Lives on in Commercial Real Estate Transactions

Caveat emptor has managed to survive in the commercial real estate sphere, as courts often presume that the contracting parties are more sophisticated than a one-time home buyer.[115] Absent contractual language that indicates otherwise, in commercial transactions, the seller generally has no duty to disclose conditions regarding the property.[116] An experienced buyer, like one who regularly partakes in commercial transactions, is presumed to know how to properly complete their due diligence, so heightened protections for these types of buyers are not necessary.[117] Courts follow the view that caveat emptor is suitable to govern "arm's length transaction[s]."[118] Unless a buyer can prove that the seller "actively concealed material and critical information" at the time of the contract, the seller has no liability.[119]

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113. *Id.* at 392.

114. *See id.*; *see also* Carter v. Cain, 490 N.Y.S.2d 472, 473 (App. Div. 1985) (holding that to remain within the protection of the common law, the builder could not live in the house for an extended period of time, stating that in this case, three years was too long, but still not clearly explaining where the line between limited occupancy and extended period of time was).

115. Karen T. Moses et al., *'Trust Me, You'll Love It': Caveat Emptor in Real Estate Transactions*, FAEGRE DRINKER (June 22, 2017), https://www.faegredrinker.com/en/insights/publications/2017/6/trust-me-youll-love-it-caveat-emptor-in-real-estate-transactions (explaining that in some jurisdictions, there are exceptions to this application to commercial transactions carved out for instances in which a seller fails to disclose issues that materially affect health and safety).

116. Devine v. Meili, 932 N.Y.S.2d 581, 583 (App. Div. 2011).

117. *Caveat Emptor: Due Diligence in Commercial Real Estate*, AM. INV. PROPS. (Sept. 7, 2016), https://aipcommercialrealestate.com/caveat-emptor (stating that "due diligence enables the purchaser to make a well-informed and conscious decision to acquire commercial property"); Moses et al., *supra* note 115.

118. Klafehn v. Morrison, 906 N.Y.S.2d 347, 348 (App. Div. 2010); *Devine*, 932 N.Y.S.2d at 582.

119. *Devine*, 932 N.Y.S.2d at 582. The court held that caveat emptor applied in a case where a buyer, after purchasing commercial property, found that the property was comprised of rotten beams and posts, a cracked foundation, and had extensive water damage which compromised the structural integrity of the building. *Id.*

III. NEW YORK'S STATUTORY HOUSING MERCHANT IMPLIED WARRANTY

This Part will address the introduction and application of Article 36-B, the current law governing the sale of newly constructed homes.[120] Subpart A will describe the legislative purpose behind Article 36-B.[121] Subpart B will discuss the specific provisions in Article 36-B.[122] Subpart C will address the effect Article 36-B has on the common law doctrine.[123] Finally, Subpart D will consider the policies that other states have adopted in dealing with new home construction.[124]

A. Introduction of a Bill Calling for the Amendment to the Real Property Law

In 1987, after numerous news articles called attention to lax practices in the home-building industry, there was a revival of interest in consumer protections specifically for new home sales.[125] The Office of the Attorney General noted that it had received an influx of complaints about the structurally defective construction of new dwellings.[126] During the New York State Assembly's 211th Session, a Bill was introduced, sponsored by Assemblyman Serano, that had the ultimate effect of repealing Section 251 of the Real Property Law ("Section 251").[127] The language of Section 251 stated that covenants were not implied in the conveyance of real property, even though New York courts were recognizing an implied warranty in the purchase of new homes.[128] The language of Section 251 was sharply at odds with recent court decisions,

120. *See infra* Part III; N.Y. GEN. BUS. LAW §§ 777–777-b (Consol. 1999).

121. *See infra* Part III.A; S. 5395-A, Reg. Sess. (N.Y. 1988); Assemb. 770-B, 211th Sess. (N.Y. 1988).

122. *See infra* Part III.B; GEN. BUS. §§ 777–777-b.

123. *See infra* Part III.C; Fumarelli v. Marsam Dev., Inc., 703 N.E.2d 251, 253 (N.Y. 1998); *see also* Caceci v. Di Canio Constr. Corp., 526 N.E.2d 266, 267 (N.Y. 1988).

124. *See infra* Part III.D.

125. N.Y. Assemb. 770-B (describing articles in the *New York Times*, *U.S. News and World Report*, and the *Wall Street Journal* that have pointed to the home-building industry for producing shoddy and defective homes); Burlingame, *supra* note 70, at 299.

126. N.Y. Assemb. 770-B; Assemb. 770-A, 211th Sess. (N.Y. 1987).

127. N.Y. REAL PROP. LAW § 251 (McKinney 2018); N.Y. Assemb. 770-A. (stating that this Bill was "an act to amend the real property law, in relation to enacting the 'new home warranty act' and repealing certain provisions thereof prohibiting implied covenants"); Burlingame, *supra* note 70, at 299-300.

128. REAL PROP. § 251; Letter from L. Paul Kehoe, Member of the Senate, State of N.Y., to Hon. Evan A. Davis, Exec. Chamber, State Capitol (Sept. 1, 1988) (on file with author) (describing that the contrast between the language of the statute and its application in the courts is why Senator Kehoe believed this legislation was especially important); N.Y. Assemb. 770-B; DeRoche v. Dame, 430 N.Y.S.2d 390, 392 (App. Div. 1980); *Caceci*, 526 N.E.2d at 270.

creating a lack of clarity about the law.[129] The provisions of the original proposal were quite different from the Bill that was eventually passed, partly because it required the creation of an issuance fund for new home purchasers that would be funded by builders.[130] It further required the State Housing Commissioner to administer a builders' registration program imposing penalties on builders who failed to register.[131]

The Bill memorandum explained that the purchase of a home is likely the "largest single investment that a family makes," but as a result of the then-current law, the families were getting less and less for their money.[132] Section 251, therefore, was an outdated law relevant to the previous century when it was uncommon for buyers to contract for both the purchase of land and the construction of a house on that land, and it was typically one or the other.[133] The Bill's supporters relied on newly enacted laws in Minnesota and New Jersey, where legislators had responded to a steady stream of complaints as to the quality of newly constructed homes.[134] The Federal Trade Commission ("FTC") was investigating new home construction and a suit brought by plaintiff purchasers around that time, the supporters noted, and the FTC Commissioner was threatening defendant home builders with federal action.[135] Almost all of the versions of the Bill included that the stated purpose was to "provide new home purchasers with certain protections lacking under existing law."[136]

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129. REAL PROP. § 251; Letter from L. Paul Kehoe to Hon. Evan A. Davis, *supra* note 128; *Caceci*, 526 N.E.2d at 270.

130. REAL PROP. § 251; N.Y. S. 5395-A; N.Y. Assemb. 770-A.

131. N.Y. Assemb. 770-A. A noticeable difference between the early versions of the Bill and the one that was later passed is that the Bill introduced to the New York Assembly in 1987 required "some funding be sought by the building code council and/or the State housing commissioner," whereas the Bill that was later introduced to the New York Senate by Senator Kehoe included no fiscal implications for state and local governments. *Id.*; N.Y. S. 5395-A.

132. N.Y. Assemb. 770-A; N.Y. Assemb. 770-B (stating that at the time, the average cost of a new home was around $63,000, but the purchaser was not getting $63,000 in quality).

133. *See* REAL PROP. § 251; N.Y. S. 5395-A; N.Y. Assemb. 770-A; N.Y. Assemb. 770-B.

134. N.Y. Assemb. 770-A; N.Y. Assemb. 770-B (describing that New Jersey legislation resulted in the operation of a state-administered warranty insurance program). The Bill's justification also indicates that Ralph Nader was vocal in urging Congress to require all builders to warrant their new homes in all states. N.Y. Assemb. 770-A; N.Y. Assemb. 770-B.

135. N.Y. Assemb. 770-A; N.Y. Assemb. 770-B (summarizing that after their investigation, the Federal Trade Commission brought suit against Kaufman & Broad Homebuilders ("K&B"), which led to K&B agreeing to furnish a warranty to all new home buyers).

136. N.Y. Assemb. 770-B (explaining that the current law provided purchasers with few safeguards and remedies). Richard Gross, Deputy Chief of the Massachusetts Attorney General's Consumer Protection Division, stated that "purchaser[s] of a new home deserve[] at least the same warranty protection as the purchaser of a new appliance" being that purchasers of a new appliance would fall under the protections of the UCC, while purchasers of a home would not. N.Y. Assemb.

Just like many other Bills, this Bill was quickly amended before it even reached the New York Senate.[137] This is when the provisions of the Bill began to take shape and resemble the current statutory protection for buyers of newly constructed homes.[138] The memorandum on the amended Bill stated that the specific provisions would include warranties "for one year freedom from defects caused by faulty workmanship and defective materials, two years freedom from defects caused by faulty installation of plumbing, electrical, heating and cooling delivery systems, and 10 years freedom from major construction defects."[139] The stated effect of the amended Bill differed from the previous version because the amended Bill did not attempt to repeal Section 251, but only to revise it.[140]

From there, the Bill was introduced to the Senate, sponsored by Senator Kehoe who believed the legislation was "especially important," as it safeguarded what were considered only basic warranties.[141] The New York Legislature discussed the Bill at length with the Home Builders Association, who eventually endorsed the Bill.[142] In the end, Section 251 was neither amended nor repealed.[143] Instead, Section 251

770-A. *But see* N.Y. S. 5395-A (stating that the justification was to "promote public confidence in the home builders trade").

137. *How a Bill Becomes a Law*, N.Y. ST. SENATE, https://www.nysenate.gov/how-bill-becomes-law-1 (last visited Aug. 1, 2021). A law is enacted in New York State once it has been adopted in "[B]ill form." *Id.* Bills are most often introduced by legislators or members of the Senate or Assembly. *Id.* Even after a Bill has been introduced, either on the Senate Floor or to the Assembly, it can be amended. *Id.* These amendments can be submitted to the Bill Drafting Commission or they can be offered on the Senate floor. *Id.* A Bill must be approved by both the Senate and the Assembly before it is sent to the Governor. *Id.*

138. *Compare* N.Y. GEN. BUS. LAW §§ 777–777-b (Consol. 1999), *with* N.Y. Assemb. 770-B (summarizing the provisions of a later amendment of the Bill that more closely resemble the current law, as it had the three-tiered warranties present in the current law and it abandoned the Warranty Insurance Program that was present in an earlier-proposed Bill).

139. *See* N.Y. Assemb. 770-B. This version of the Bill became known as 770-B, as opposed to the earlier version called 770-A, because when a Bill is amended, it retains its original number, but the amended versions are denoted by a different letter such as A, B, C, D, and so on. N.Y. Assemb. 770-A; N.Y. Assemb. 770-B; *How a Bill Becomes a Law*, *supra* note 137.

140. N.Y. Assemb. 770-B (stating that under this Bill, "covenants would not be implied in any conveyance of real property, except as the Bill would provide"). *Compare* N.Y. Assemb. 770-A, *with* N.Y. Assemb. 770-B (explaining that the memorandum for the amended version of the Bill and the initially proposed version of the Bill contained the same "justification" and "purpose").

141. Letter from L. Paul Kehoe to Hon. Evan A. Davis, *supra* note 128. Senator Kehoe was a Republican from the 53rd District. *187th New York State Legislature*, WIKIPEDIA, https://en.wikipedia.org/wiki/187th_New_York_State_Legislature (last visited Aug. 1, 2021).

142. Letter from L. Paul Kehoe to Hon. Evan A. Davis, *supra* note 128; Memorandum in Support from the New York State Builders Assoc., Inc. (on file with author); Letter from Robert A. Wieboldt, Exec. Vice President, New York State Builders Assoc., Inc., to Hon. Evan A. Davis, Exec. Chamber, State Capitol (Sept. 1, 1988) (on file with author).

143. *See* Memorandum from Robert Abrams, Att'y Gen., State of New York Dep't of L., to the Governor (Aug. 29, 1998) (on file with author).

applied only to title covenants.[144] The Bill continued to take shape into what is now the current law, Article 36-B, which specifically governs the sale of newly constructed homes.[145] Then Attorney General, Robert Abrams, explained that the Bill mirrored both the UCC's warranties for the sale of goods and the Home Owners Warranty ("H.O.W.").[146] The H.O.W. was a voluntary warranty-insurance program common in the home-building industry.[147] The Bill received wide support from New York Senators and Assemblymen, with only one single Assemblyman voting "nay."[148]

A criticism of the new Bill by the Attorney General was that it did not include an insurance program or general security fund, and that it lacked teeth because it failed to provide specific private and public enforcement remedies.[149] An insurance program was crucial, the Attorney General explained, because it would ensure that a builder's insolvency would not act as a bar to recovery of damages.[150] Nonetheless, his office and the State Consumer Protection Board urged for the Bill's approval.[151]

The New York State Builders Association was a fierce proponent of the Bill and wrote a lengthy letter and memorandum to the Governor supporting its approval.[152] Without legislative clarification of *Caceci*, which this Bill provided, the courts would supply clarification, adding

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144. *See* N.Y. S. 5395-A.

145. *See id.*

146. Memorandum from Robert Abrams to the Governor, *supra* note 143 (explaining that the Home Owners Warranty ("H.O.W.") Program covered major structural defects for ten years, which was four years longer than Article 36-B). Like Article 36-B, the H.O.W. Program protected subsequent owners so long as it fell within the unexpired warranty period. *Id.* In the memorandum to the Governor, the Attorney General argued that although new home warranty protections offered by H.O.W. and other programs had been questioned by the *New York Times*, the protections were necessary for consumer protections. *Id.*

147. Memorandum from Robert Abrams to the Governor, *supra* note 143.

148. *See, e.g.*, N.Y. S. 5395-A.

149. *See* Memorandum from Robert Abrams to the Governor, *supra* note 143 (arguing that these deficiencies must be corrected to make the New York Bill more like New Jersey's "New Home Warranty and Builders' Legislation Act"). The Attorney General stated that for many years, he urged New York to adopt legislation similar to the legislation in place in New Jersey, which created statutory warranties secured by a program of insurance. *Id.*

150. Memorandum from Robert Abrams to the Governor, *supra* note 143.

151. *Id.*; *see also* Memorandum from Jean Miller, General Couns., State Consumer Prot. Bd., to Evan A. Davis, Couns. to the Governor (Sept. 1, 1988) (on file with author).

152. Letter from Robert A. Wieboldt to Hon. Evan A. Davis, *supra* note 142; Memorandum in Support from the New York Builders Assoc., Inc., *supra* note 142. The New York State Builders Association explained that the purpose of this Bill was to "stimulate warranty competition among sellers in the marketplace and to provide better information to consumers." Letter from Robert A. Wieboldt to Hon. Evan A. Davis, *supra* note 142. Wieboldt stated that the Bill answered important questions about new home warranties with "practicality and fairness" by creating a "reasonably clear, detailed" set of warranty rules. *Id.*

tremendous risk because this would take a longer amount of time.[153] The New York State Builders Association argued that while courts were slowly clarifying the common law Housing Merchant Doctrine on a case-by-case basis, builders would be "disinclined" to provide express warranties to their customers because they would "recogniz[e] the cost and complexity of litigation for new home buyers" and take advantage of this.[154] The home-building industry at the time was a $2.5 billion per year enterprise and without this legislation, Weiboldt argued, buyers and sellers would overwhelm the court system with cases involving questions that could have been easily settled by legislation.[155]

The Office of Business Permits and Regulatory Assistance stood alone in writing a memorandum to the Governor recommending disapproval of the Bill.[156] Assistant Counsel for this Office, Joanne E. Jenkins, stated that although the Bill appeared to protect "buyer[s] of [] new home[s] from a builder who [had] construct[ed] the home with defects," it actually acted as a means for builders to limit their liability.[157] The flaw in the Bill stemmed from a provision allowing the builder to exclude or modify the warranty and provide only a limited warranty.[158] This limited warranty would only require the builder to construct the home in accordance with applicable building code

153. Memorandum in Support from the New York Builders Assoc., Inc., *supra* note 142; Letter from Robert A. Wieboldt to Hon. Evan A. Davis, *supra* note 142 (explaining that the Bill's definition section would be effective in clarifying many of the unanswered questions from *Caceci v. Di Canio Construction Corporation*); Caceci v. Di Canio Constr. Corp., 526 N.E.2d 266, 270 (N.Y. 1988).

154. Memorandum in Support from the New York Builders Assoc., Inc., *supra* note 142. The New York State Builders Association stated that the following issues were unclear under *Caceci v. Di Canio Construction Corporation*:

> [T]he types of construction affected, the elements of the home that are covered or excluded, the identification of the warrantor or warrantors, the standards to be applied for measurement of defects, whether coverage extends to successors in title or others not in privity with the seller, the consumer's obligations under the warranty, the warrantor's duties in the event of a defect, the remedies for breach and the measure of damages, the statute of limitations for claims, third party actions for indemnification or contribution, coordination with other state and local laws, and the ability of parties to modify, waive or supersede the implied warranty.

Letter from Robert A. Wieboldt to Hon. Evan A. Davis, *supra* note 142.

155. Letter from Robert A. Wieboldt to Hon. Evan A. Davis, *supra* note 142. The New York State Builders Association stated that laws for an industry this large should not be left uncertain or left to be resolved in a slow case-by-case manner "in which particular facts and circumstances rather than general policy considerations may be determinative." *Id.*

156. Letter from Joanne E. Jenkins, Assistant Couns., Off. of Bus. Permits & Regul. Assistance, to Hon. Evan A. Davis, Couns. to the Governor, Exec. Chamber (Aug. 31, 1988) (on file with author).

157. *Id.*

158. *Id.*

standards, something that the builder already had to do.[159] According to the Office of Business Permits and Regulatory Assistance, this provision served as a statutory opt-out in favor of the builder rather than as a mechanism to protect a buyer.[160] The memorandum suggested that it is more reasonable to leave such limitations on builder liability to contract negotiations rather than to guarantee them by legislation.[161] However, these observations and objections were not weighed and certainly did not prevail.[162]

B. Article 36-B Became Law in 1989

Two months later, Article 36-B was signed into law.[163] New York amended the General Business Laws by adding this new article, which included a statutory protection for buyers of newly constructed homes.[164] Article 36-B became effective in 1989.[165] The relevant portions of the Article 36-B Section 777-a are organized as follows:

> 1. Notwithstanding the provisions of section two hundred fifty-one of the real property law, a housing merchant implied warranty is implied in the contract or agreement for the sale of a new home and shall survive the passing of title. A housing merchant implied warranty shall mean that:
> a. one year from and after the warranty date the home will be free from defects due to a failure to have been constructed in a skillful manner;
> b. two years from and after the warranty date the plumbing, electrical, heating, cooling and ventilation systems of the home will be free from defects due to a failure by the builder to have installed such systems in a skillful manner; and
> c. six years from and after the warranty date the home will be free from material defects.
> 2. Unless the contract or agreement by its terms clearly evidences a different intention of the seller, a housing merchant implied warranty does not extend to:

159. *Id.*
160. *Id.*
161. *Id.*
162. *Id.*
163. N.Y. GEN. BUS. LAW §§ 777–777-b (Consol. 1999); 1988 N.Y. Sess. Laws 2-4 (McKinney); Burlingame, *supra* note 70, at 299-300.
164. *See, e.g.*, GEN. BUS. §§ 777–777-b; Losito, *supra* note 83, at 377; John Caravella, *The Implied Warranty on the Sale of New Homes: What Homeowners & Contractors Need to Know*, THE L. OFFS. OF JOHN CARVELLA, P.C.: CONSTR. L. BLOG (Dec. 20, 2019), https://www.liconstructionlaw.com/construction/implied-warranty-sale-new-homes-homeowners-contractors-need-know (stating that the New York statute softened the traditional maxim of "let the buyer beware" with a warranty that works in favor of the buyer).
165. *See* GEN. BUS. §§ 777–777-b; *see also* 1988 N.Y. Sess. Laws at 2-4.

> a. any defect that does not constitute (i) defective workmanship by the builder or by an agent, employee or subcontractor of the builder, (ii) defective materials supplied by the builder or by an agent, employee or subcontractor of the builder, or (iii) defective design provided by a design professional retained exclusively by the builder; or
> b. any patent defect which an examination ought in the circumstances to have revealed, when the buyer before taking title or accepting construction as complete has examined the home as fully as the buyer desired, or has refused to examine the home.[166]

The implied warranties provided for in Article 36-B "survive[] after the closing on the property."[167] In addition, Article 36-B Section 777-a lays out specific procedures that a buyer must follow before they can sue the builder of their home.[168] This procedural roadmap contains time limitations, damage calculations, and condition precedents, without which, the buyer cannot assert a claim against the builder.[169] These provisions currently govern newly constructed homes.[170] Article 36-B Section 777-a(4) states:

> 4.a. Written notice of a warranty claim for breach of a housing merchant implied warranty must be received by the builder prior to the commencement of any action under paragraph b of this subdivision and no later than thirty days after the expiration of the applicable warranty period, as described in subdivision one of this section. The owner and occupant of the home shall afford the builder reasonable opportunity to inspect, test and repair the portion of the home to which the warranty claim relates.
> b. An action for damages or other relief caused by the breach of a housing merchant implied warranty may be commenced prior to the expiration of one year after the applicable warranty period, as described in subdivision one of this section, or within four years after the warranty date, whichever is later. In addition to the foregoing, if

166. *See* GEN. BUS. § 777-a; Iarlawtv, *What Implied Warranties Are There from a Builder of New Residential Construction in New York*, YOUTUBE (Sept. 3, 2011), https://www.youtube.com/watch?v=pWJndGnZifE.

167. LYNN T. SLOSSBERG, THE ESSENTIALS OF REAL ESTATE LAW 571 (3d ed. 2015).

168. GEN. BUS. § 777-a; Rushford v. Facteau, 669 N.Y.S.2d 681, 682 (App. Div. 1998); VINCENT DI LORENZO, NEW YORK CONDOMINIUM AND COOPERATIVE LAW § 5:14 (2d ed. 2020). If a plaintiff does not follow the procedural rules set out in Section 777-a(4), such as the notice and limitation period, their claim against a builder could be barred. JOSEPH L. MARINO, WEST'S MCKINNEY'S FORMS REAL PROPERTY PRACTICE § 3:164 (2020).

169. GEN. BUS. § 777-a; Finnegan v. Brooke Hill, LLC, 833 N.Y.S.2d 107, 108-09 (App. Div. 2007); Trificana v. Carrier, 916 N.Y.S.2d 399, 400 (App. Div. 2011); MARINO, *supra* note 168, at § 3:164 (explaining that while the notice provision in Section 777-a(4)(a) is a condition precedent, giving the builder a "reasonable opportunity to inspect, test and repair" the portion of the home in question is not a condition precedent to bringing a claim, but can be used as an affirmative defense).

170. GEN. BUS. §§ 777–777-b.

> the builder makes repairs in response to a warranty claim under paragraph a of this subdivision, an action with respect to such claim may be commenced within one year after the last date on which such repairs are performed. The measure of damages shall be the reasonable cost of repair or replacement and property damage to the home proximately caused by the breach of warranty, not to exceed the replacement cost of the home exclusive of the value of the land, unless the court finds that, under the circumstances, the diminution in value of the home caused by the defect is a more equitable measure of damages. c. In addition to any other period for the commencement of an action permitted by law, an action for contribution or indemnification may be commenced at any time prior to the expiration of one year after the entry of judgment in an action for damages under paragraph b of this subdivision.[171]

Article 36-B Section 777 contains a definition section of many of the terms in the statute, but these definitions have been strongly criticized for defining these terms too narrowly.[172] For example, "new home" is defined as a "single family house or for sale unit in a multi residential structure of five stories or less."[173] A "custom home," which is the object of a contract between the current owner of the property seeking a new home on that same property and the contractor who will provide the new home, is not considered a "new home" within the statutory definition, thus, custom homes fall outside of statutory protections.[174] Within the context of the statute, "skillful manner" means that "workmanship and materials meet or exceed the specific standards of applicable building code[,]" and if there are no applicable building codes, then they simply must meet "standards of locally accepted building practices."[175] Many argue that Article 36-B ensures only "minimal safety standards" and is too narrow to protect consumers'

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171. *See* GEN. BUS. § 777-a.

172. JOLINA C. CUARESMA ET AL., CONSUMER PROTECTION AND THE LAW § 18:25 (2020 ed. 2019); Christian Murray, *Dreams on Hold/Tempers and Down Payments May Be Lost in Builder-Buyer Squabbles*, NEWSDAY (Oct. 31, 2002), https://www.newsday.com/classifieds/real-estate/dreams-on-hold-tempers-and-down-payments-may-be-lost-in-builder-buyer-squabbles-1.303860.

173. GEN. BUS. § 777; Bd. of Managers of Beacon Tower Condo. v. 85 Adams St., LLC, 25 N.Y.S.3d 233, 238 (App. Div. 2016).

174. Watt v. Irish, 708 N.Y.S.2d 264, 267 (Sup. Ct. 2000) (holding that custom homes are not included in the definition of "new home"); Tripodianos, *supra* note 24 (arguing that although custom homes are excluded from protection, there is a growing trend in the courts that Article 38-B will apply to custom homes in the future). *But see* Gorsky v. Triou's Custom Homes, Inc., 755 N.Y.S.2d 197, 205, 207-08 (Sup. Ct. 2002) (holding that a custom home does fall within statutory protections).

175. GEN. BUS. § 777.

reasonable expectations about the quality of the home.[176] Under Article 36-B, a builder need only conform to statewide uniform building codes, not to local building codes, which calls into question the purposes of local building codes, which normally have stricter standards, as they are specific to the municipality.[177]

In addition, the statute does provide the opportunity for buyers and sellers to agree to modify or waive Article 36-B's warranties through "clear and conspicuous terms," which is counterproductive to the legislative purpose of protecting buyers.[178] In Article 36-B Section 777-b, the statute provides that certain minimums must be met, so as to ensure that the buyer is not being taken advantage of.[179] Some of the express requirements that must be met if the seller is looking to provide a limited warranty are that a "copy of the express terms of the limited warranty shall be provided in writing to the buyer" prior to the execution of the contract, a copy of the express terms have to be "incorporated in[] the contract," and the language of the contract must "mention the housing merchant implied warranty" and that this limited warranty is excluding the implied warranty.[180] The statute says that all these provisions must be written in "plain English."[181] Article 36-B Section 777-b provides an example of what "clear and conspicuous" plain English could look like: "[T]here are no warranties which extend beyond the face hereof."[182] While this was a good attempt to create clarity, many people argue that any language aside from this example will result in litigation.[183] Article 36-B Section 777-b(4) also clearly explains what specific information must be included in the limited warranty for it to exclude the housing merchant implied warranty.[184] It states:

> 4. A limited warranty sufficient to exclude or modify a housing merchant implied warranty must be written in plain English and must clearly disclose:
> a. that the warranty is a limited warranty which limits implied warranties on the sale of the home; the words "limited warranty" must

176. McDaniel, *supra* note 11, at 769; CUARESMA ET AL., *supra* note 172, § 18:25.

177. *See* McDaniel, *supra* note 11, at 769; *see also* CUARESMA ET AL., *supra* note 172, § 18:25.

178. GEN. BUS. § 777-b; Stephen M. Lasser, *Bringing a Construction Defect Claim*, COOPERATOR NEWS N.Y. (Aug. 2016), https://cooperator.com/article/bringing-a-construction-defect-claim/full (explaining that Section 777-b permits the parties to exclude the housing merchant implied warranty in favor of a "limited warranty").

179. GEN. BUS. § 777-b; Latiuk v. Faber Constr. Co., 703 N.Y.S.2d 645, 645 (App. Div. 2000).

180. GEN. BUS. § 777-b; *Latiuk*, 703 N.Y.S.2d at 645.

181. *See* GEN. BUS. § 777-b.

182. *See id.*

183. Cummings, *supra* note 22, at 64.

184. GEN. BUS. § 777-b(4).

be clearly and conspicuously captioned at the beginning of the warranty document;

b. the identification of the names and addresses of all warrantors;

c. the identification of the party or parties to whom the warranty is extended and whether it is extended to subsequent owners; the limited warranty must be extended to the first owner of the home and survive the passing of title but may exclude any or all subsequent owners;

d. a statement of the products or parts covered by the limited warranty;

e. the clear and conspicuous identification of any parts or portions of the home or premises that are excepted or excluded from warranty coverage, and the standards that will be used to determine whether a defect has occurred; provided, however, that:

i. any exception, exclusion or standard which does not meet or exceed a relevant specific standard of the applicable building code, or in the absence of such relevant specific standard a locally accepted building practice, shall be void as contrary to public policy and shall be deemed to establish the applicable building code standard or locally accepted building practice as the warranty standard; and

ii. any exception, exclusion or standard that fails to ensure that the home is habitable, by permitting conditions to exist which render the home unsafe, shall be void as contrary to public policy.

f. what the builder and any other warrantor will do when a defect covered by the warranty does arise, and the time within which the builder and any other warrantor will act;

g. the term of the warranty coverage and when the term begins, provided, however, that such term shall be equal to or exceed the warranty periods of a housing merchant implied warranty, as defined in subdivision one of section seven hundred seventy-seven-a of this article;

h. step-by-step claims procedures required to be undertaken by the owner, if any, including directions for notification of the builder and any other warrantor; an owner shall not be required to submit to binding arbitration or to pay any fee or charge for participation in nonbinding arbitration or any mediation process;

i. any limitations on or exclusions of consequential or incidental damages, and any limitations on the builder's and other warrantor's total liability, conspicuously expressed on the first page of the warranty. Notwithstanding the foregoing, a limited warranty shall not be construed to permit any limitation on or exclusion of property damage to the home proximately caused by a breach of the limited warranty, where the court finds that such limitation or exclusion would cause the limited warranty to fail of its essential purpose, except that such property damage may be limited by an express limitation on the

> builder's or other warrantor's total liability in accordance with the provisions of this paragraph.[185]

Critics of Article 36-B argue that the "weakest link in the New York law is the builder's ability to disclaim the warranty."[186] Many builders utilize this provision and substitute a limited warranty that includes a cap on the amount they will warrant, leaving the buyers in a very vulnerable position if they have a defective house that runs fees above that cap.[187] This is the same concern raised by the Director of the Office of Business Permits and Regulatory Assistance back in 1988 in her disapproval of the Bill proposal for Article 36-B.[188]

What the statute does not address are the types, if any, of protections guaranteed to a buyer of a flipped home, nor does it envision the possibility of a home becoming statutory "new property" as a result of its purchase by a professional flipper.[189] The statute's vague definitions and language give builder-vendors the opportunity to try to find "loopholes" in coverage by arguing that "new home" should take on the plain meaning of the word, as opposed to being inclusive of all the types of property that put buyers at a higher risk.[190] Many builders argue for a reading of the statute that ignores the fact that oftentimes in the process of being flipped, the home will be "gutted, destroyed, or demolished to the foundation," potentially putting buyers at the very same increased risks that Article 36-B was meant to protect against.[191]

C. New York Statutory Housing Merchant Implied Warranty Supplants the Common Law, Repealing Any Common-Law Remedies Formerly Available to Buyers

In *Fumarelli v. Marsam Development, Inc.*,[192] the court held that the statutorily implied warranties are exclusive and act as a complete substitute for the common-law remedy established in *DeRoche* and

185. *Id.*

186. Jay Romano, *Your Home; Warranties For New Houses,* N.Y. TIMES, July 30, 2000, at 3, 9 (explaining that many lawyers do not like dealing with new construction contracts because the provision that allows the seller to modify or get rid of the implied warranty makes these types of contracts very complicated).

187. *Id.*

188. Letter from Joanne E. Jenkins to Hon. Evan A. Davis, *supra* note 156.

189. Cummings, *supra* note 22, at 57 (stating that the statute's broadly defined terms leave open the possibility for litigation regarding "renovated homes, nonresidential property converted to residential use, and mixed use property.").

190. *See id.* at 58.

191. Cotton, *supra* note 71, at 268.

192. 703 N.E.2d 251 (N.Y. 1998).

Caceci.[193] The court held that Article 36-B was a "full, effective and realistic substitute" for the common law and stated that the legislature did not intend an "overlapping dual track."[194] This decision left purchasers of newly constructed residential homes in buildings of six or more stories completely unprotected, outside of contract, as they no longer fell under the protections of either the common law or the statutory protections of Article 36-B.[195]

D. Are Buyers of Flipped Properties in New York More or Less Protected Than Buyers in Other States?

Across the nation, states have slowly followed the same pattern of shifting away from caveat emptor, but they have taken different approaches in their statutory provisions.[196] This Subpart will examine several different state laws with regard to warranties for new home construction.[197] It will also address the criticisms to each state's policies when applicable.[198]

1. Florida's Essential Services Test

In Florida, courts apply an "essential services test" in determining the scope of the implied warranty of habitability to protect buyers of new home construction; this is the common law rule.[199] This test asks: "[W]hether, 'in the absence of the service, is the home inhabitable, that is, is it an improvement providing a service essential to the habitability of the home?'"[200] If yes, then the warranty applies.[201] Florida previously

193. *See id.* at 253; Caceci v. Di Canio Constr. Corp., 526 N.E.2d 266, 267 (N.Y. 1988); DeRoche v. Dame, 430 N.Y.S.2d 390, 392 (App. Div. 1980); *see also* DI LORENZO, *supra* note 168, § 5:14.

194. *Fumarelli*, 703 N.E.2d at 253, 256 (stating that such an "overlapping dual track" would cause "confusion, indefiniteness, and lawsuits"); Randy Sutton, Annotation, *Validity, Construction, and Application of New Home Warranty Acts*, 101 A.L.R.5th 477 § 10 (2002).

195. Bd. of Managers of Beacon Tower Condo. v. 85 Adams St., LLC, 25 N.Y.S.3d 233, 236, 238 (App. Div. 2016) (explaining that the buyer of a unit in a condominium apartment building, with twenty-three stories and seventy-nine units in it, had no remedy after the amendment to the New York statute).

196. Edward V. Crites & Joseph C. Blanner, *Builders Beware: Strict Liability for Hidden Defects in New Homes*, 72 J. MO. BAR 12, 12 (2016) (describing that states across the country have moved away from the strict enforcement of caveat emptor); French, *supra* note 35, at 945-47 (describing the different ways in which some states, including Florida, Minnesota, Indiana, Louisiana, and Virginia, to name a few, have approached providing protections for buyers).

197. *See infra* Part III.D.1–3; French, *supra* note 35, at 945-47.

198. *See infra* Part III.D.1–3; McKernan, *supra* note 31, at 386.

199. *See* French, *supra* note 35, at 936.

200. *See id.*

201. *See id.*

applied a statutory rule which stated that to establish a cause of action alleging breach of the implied warranty under Section 553.835, a buyer must demonstrate that: "(1) the claim is regarding a new home[;] (2) the claim is with regard to damage to the home or a structure or improvement on or under the home's lot[;] and (3) the complained of improvement or structure immediately and directly supports the habitability of the home."[202]

2. Arizona's Implied Warranty of Habitability

In Arizona, the courts also recognize an implied warranty of habitability and workmanship for new home construction.[203] After looking to Illinois court decisions, Arizona courts held that their implied warranty of habitability could be more accurately understood as a warranty of fitness for a particular purpose, meaning that "the mere fact that the house is capable of being inhabited does not satisfy the implied warranty."[204] The courts stated that the applicable standard for determining whether or not there is a breach of warranty is one of "reasonableness, in light of all surrounding circumstances."[205] The court examines factors such as the age of the home, its maintenance, and the use to which it has been put.[206] Like Article 36-B, Arizona courts have recognized the rights of subsequent purchasers under the implied warranty, stating that contract privity is not required.[207]

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202. *Id.* at 939-41 (stating that the previous statutory warranty was found to be unconstitutional, and Florida reverted back to the common law warranty that favored buyers). Florida courts felt that essential services closely affect the habitability of a home, so the common law essential services test was a better way to keep builders, who were in the "best position to know" about defects, honest. *Id.*

203. *See* McKernan, *supra* note 31, at 385.

204. *Id.*; Petersen v. Hubschman Constr. Co., 389 N.E.2d 1154, 1158 (Ill. 1979). The Illinois Supreme Court held that there was a breach of implied warranty of habitability for plaintiffs who had contracted for the construction of a new home, even though it noted that the house was habitable and did not pose a dangerously unsafe condition. *Id.* at 1159-60.

205. McKernan, *supra* note 31, at 386.

206. *Id.* (explaining that the defendant builder still has the opportunity to prove that the plaintiff's losses were the result of the plaintiff's own failure to take a reasonable course of action); Richards v. Powercraft Homes, Inc., 678 P.2d 427, 430 (Ariz. 1984).

207. McKernan, *supra* note 31, at 386. Arizona courts have held that latent defects in a newly constructed home are just as detrimental to subsequent buyers as they are to the original buyer. *Id.* Because the builder "is in a better position than a subsequent owner to prevent the occurrence of major defects," the same logic is applied to warranties for subsequent buyers of new home construction, and the costs of poor workmanship are borne by the builders. *Id.* Arizona courts have not yet decided whether a disclaimer or modification of the implied warranty by the original purchaser can be held as consistent with public policy, nor have they decided whether such a disclaimer would be binding on a subsequent purchaser. *Id.* at 387-88.

Arizona's implied warranty is not boundless and the courts have recognized limitations.[208] The Arizona courts have a statute of limitations specific to actions arising out of new home construction contracts, stating that "no action based in contract may be maintained against a person who develops and sells real property more than eight to nine years after the substantial completion of construction."[209] Another limitation to the Arizona warranty is that the purchaser must show that he or she made a reasonable inspection of the home before he or she may recover.[210]

3. New Jersey's New Home Warranty and Builders' Registration Act

New Jersey's New Home Warranty and Builders Registration Act is similar to Article 36-B in that it is divided into three coverage periods.[211] For one year, the warranty covers defects "caused by faulty workmanship and defective materials due to noncompliance with . . . building standards."[212] For two years, the warranty covers "defects caused by faulty installation of plumbing, electrical, heating and cooling delivery systems."[213] Finally, for ten years, the home is warranted from "major construction defects."[214] Another provision of the Act requires that builders register with the Department of Community

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208. *Id.* at 386-87.

209. *Id.* (explaining that this statute of limitations also applies to subsequent purchasers).

210. *Id.* at 387. This limitation is criticized because scholars argue that this will greatly hurt buyers who are moving to Arizona from out of state and do not have the opportunity or do not know that they need to have such an inspection done in order to be protected by this warranty. *Id.*

211. Cotton, *supra* note 71, at 269 (stating that warranty provisions are "most expansive" in the first year). New Jersey was the first state to provide a warranty system for new home construction and the intent was to "protect new homeowners and to legislatively abandon caveat emptor." *Id.* at 267. New Jersey's Act is also similar to Section 777 because the warranty extends to the subsequent purchasers, so long as it is still during the warranty period; privity between the builder and the subsequent purchaser is not required. *Id.* at 270; N.Y. GEN. BUS. LAW §§ 777–777-b (Consol. 1999).

212. Cotton, *supra* note 71, at 269. Problems that typically fall within the reach of the first-year warranty coverage include "problems with landscaping; masonry and carpentry; roofing and roofing systems; doors and windows; hard surface flooring; and specialty items (e.g., fireplaces)." *Id.*

213. *Id.*

214. *Id.* "A major construction defect is defined by the Act as 'any actual damage to the load bearing portion of the home including damage due to subsistence, expansion or lateral movement of the soil . . . which affects its load bearing function and which vitally affects or is imminently likely to vitally affect use of the home for residential purposes.'" *Id.* at 269-70. "Defective items resulting in the 'failure of the load-bearing portion of a new home' typically include 'the framing members and structural elements . . . [such as] roof rafters and trusses, ceiling and floor joists, bearing partitions, [and] supporting beams.'" *Id.* at 270.

Affairs and participate in the warranty system.[215] Builders must either join in the new home warranty security fund, where they will contribute a specified percentage of the sale price of the home to the fund, or they must provide an appropriate alternative.[216] The purpose of this provision is to ensure that homeowners who have successful claims will be paid, even if a builder has no money to pay the claim.[217] Finally, under this Act, all homeowners are given a manual at closing that explains the warranty and the process of bringing a claim.[218]

Many critics of New Jersey's warranty system take issue with the language of the actual statute, stating that there is disagreement over "what constitutes a 'major construction defect,' what is covered by the warranty, and what an election of remedies is under the Act."[219] The "obtuse" language of the Act, paired with New Jersey's inconsistent case law, makes it hard for buyers and sellers to come to a consensus on what "major construction defect" means.[220] In addition, there are complaints about a provision of the Act that exempts from coverage a claim that stems from "negligent or improper maintenance" by the homeowner.[221] This provision has been strictly construed against homeowners in defeating their claims and seemingly discourages the "proactive homeowner" who is forced to work through the slow process of the Act, instead of attempting to quickly handle a defect in their home themselves.[222]

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215. *Id.* at 268 (explaining that participation is mandatory for builders and "no builder shall engage in the business of constructing new homes" until they are registered).

216. *Id.* at 268-69. The specified percentage of the sale that a builder has to pay into the fund varies depending on the number of successful claims that have been brought against the builder, so the Act incentivizes the builders to settle claims with buyers outside of court in order to keep their specified percentage lower. *Id.*

217. *Id.* at 268.

218. *Id.* at 269.

219. *Id.* at 267-68. This Act has "fallen into such disrepute" that a trial judge in New Jersey called it "a useless piece of paper" because it has failed to fulfill its objectives. *Id*. at 268. Some people in New Jersey suggest adopting a similar provision to Pennsylvania's New Home Construction Consumer Bill, which makes it fraudulent for a builder who has entered into a homebuilding contract to "change the name of the home building business, liability insurance information, the home builder's address or any other identifying information without advising the consumer in writing within ten days of any such change." *Id.* at 275. It is argued that this addition would pair well with the registration provision already in place in New Jersey, because it would help keep track of builders who walk away from unfinished jobs and help keep better track of claims against the builders. *Id*.

220. *Id.* The legislature has tried to remedy this problem by clarifying in an amendment that a "major construction defect" includes "any substantial failure to meet applicable structural requirements." *Id.* at 276.

221. *Id.* at 271.

222. *Id.*

IV. NEW YORK'S ARTICLE 36-B SHOULD BE AMENDED

New York's statutory protections fall short when applied to the current real estate climate.[223] Although the statute defines "new home" in the definition section, it does not define the term within the context of houses that are purchased and "gutted" with the intent to sell quickly for profit.[224] With buyers of flipped properties in mind, this Part will propose an amendment to Article 36-B that will create a bright-line rule for New York's implied warranties of new home construction.[225]

The proposed amendment will have three parts.[226] First, as suggested in Subpart A, the statute should be amended to define "new home" as any residential dwelling where the premises have been rehabilitated, gutted, destroyed, or demolished by a builder, with the intent to resell the home to a buyer, rather than to keep and live in themselves.[227] Second, as explained in Subpart B, there will be a provision added that will explain warranty coverage under the 25/50 rule.[228] Third, as described in Subpart C, there will be additional language added to the statute that specifically defines and addresses individuals or other investors who "flip" homes for a living.[229] Each Subpart will discuss the benefits that accrue and the issues that could arise from the application of these amendments.[230]

A. Altered Definition of New Construction

Article 36-B Section 777's definition of "new home" or "home" completely excludes one of the most important contemporary applications of this statute: flipped houses.[231] Although much of the language included in the definition is helpful in sorting out what types of property are not covered, it fails to adequately explain what is covered, leaving buyers and sellers with too much uncertainty.[232] By adding language stating that a "new home" includes, but is not limited to,

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223. *See* Younes, *supra* note 36 (describing the 8.6% increase in house flips in the New York City area between 2016 and 2017).

224. N.Y. GEN. BUS. LAW § 777 (Consol. 1999); Cotton, *supra* note 71, at 268.

225. *See infra* Part IV; Cummings, *supra* note 22, at 51 (explaining that New York's statutory warranty is inherently weak as a result of its broad drafting).

226. GEN. BUS. § 777.

227. *See infra* Part IV.A; GEN. BUS. § 777; Cotton, *supra* note 71, at 268.

228. *See infra* Part IV.B; ROBERT C. ELLICKSON ET AL., LAND USE CONTROLS: CASES AND MATERIALS 472 (5th ed. 2020).

229. *See infra* Part IV.C; Younes, *supra* note 36 (describing the definition of "flipping a home").

230. *See infra* Part IV.A–C; Cummings, *supra* note 22, at 51.

231. GEN. BUS. § 777; Younes, *supra* note 36.

232. *See* GEN. BUS. § 777.

premises that have been purchased, and then rehabilitated, gutted, destroyed, or demolished by a builder with the intent to renovate and resell those premises, rather than to keep and live there themselves, flipped homes will come within the statutory definition of a "new home" or "home."[233] The proposed amendment would remove the current language in Article 36-B Section 777 that limits new home construction to "for-sale units in building[s] of [five] stories or less," because it is prejudicial to buyers in more highly populated areas and should not be determinative in the assessment of a "new home."[234]

These changes will not affect other types of "new home" construction that are not addressed by this Note, but will act only to expand the warranty to the types of homes that are currently not included, despite the need for heightened warranties.[235] This addition will resolve any question about whether a flipped house falls within the category of "new home" and whether Article 36-B protects the buyers of these homes.[236] A possible wrinkle in these alterations is that the warranty will be too broad and, therefore, unmanageable for builders.[237] Although the purpose of these amendments is to create more protections for buyers, it would not be beneficial to the house-flipping market to create an overly extensive warranty that tips the scale too far in favor of the buyers.[238] If the statutory warranty is more inclusive of the types of property to be covered, it can allow for coverage of warranty to be based on the magnitude of the rehabilitation, which is a more logical way to determine what homes are putting buyers at heightened risk and require heightened seller accountability.[239] This is where the 25/50 rule comes in.[240]

B. 25/50 Rule for Warranty Coverage

The next amendment to Article 36-B is the introduction of the 25/50 rule, which will determine whether a "new home" or how much of a "new home" is warranted based on how significant the rehabilitation was.[241] If the cost of renovations exceeds fifty percent of the building's

233. Cotton, *supra* note 71, at 268.
234. *See* GEN. BUS. §§ 777–777-b.
235. *Id.*
236. *Id.*
237. *Id.*; McDaniel, *supra* note 11, at 764.
238. DeRoche v. Dame, 430 N.Y.S.2d 390, 392 (App. Div. 1980); McDaniel, *supra* note 11, at 764.
239. ELLICKSON ET AL., *supra* note 228, at 472.
240. *Id.*
241. *Id.*

total value, then Article 36-B's protections will extend to the entire home.[242] If the renovations' total is between twenty-five and fifty percent of the building's total value, then the warranties apply only to the renovated portions of the home.[243] If the total cost of the renovations is less than twenty-five percent of the home's total value, then whether the warranty applies to that particular renovated portion of the home will be decided on a case-by-case basis.[244] Factors to be considered when a court is determining whether such a rehabilitation justifies the warranties of Article 36-B can include the effect of the defect on the use of the home, the age of the home, its maintenance, the use to which it has been put, whether or not the service rendered by the investor was essential to the use of the home, etc.[245]

The rationale for the 25/50 rule's application when determining which homes will fall within the three-tier coverage of Article 36-B is that more significant renovations warrant more significant protections.[246] If less than fifty percent of a home has been affected, it is excessive for the entire home to be covered by these warranties, as that could result in a seller being held liable for a defect in a portion of the house he or she never changed.[247] This will also encourage flippers to be more reserved with their projects and only take on what they realistically think they can successfully complete.[248] Investors may be incentivized to take on smaller, more manageable projects, as that would result in fewer warranties that are implied to their buyers.[249]

C. Builder Addressed

Finally, Article 36-B Section 777's definition for "builder" will be expanded to include language describing people or entities who buy houses with the intent to rehabilitate or renovate and then resell.[250]

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242. *Id.*; GEN. BUS. §§ 777–777-b.

243. ELLICKSON ET AL., *supra* note 228, at 472; GEN. BUS. §§ 777–777-b.

244. ELLICKSON ET AL., *supra* note 228, at 472; GEN. BUS. §§ 777–777-b.

245. McKernan, *supra* note 31, at 386.

246. ELLICKSON ET AL., *supra* note 228, at 472; GEN. BUS. §§ 777–777-b.

247. ELLICKSON ET AL., *supra* note 228, at 472; GEN. BUS. §§ 777–777-b.

248. ELLICKSON ET AL., *supra* note 228, at 472; Brown, *supra* note 75.

249. ELLICKSON ET AL., *supra* note 228, at 472 (explaining that the 25/50 rule has been used by code officials to determine how codes should apply to an existing building that was undergoing rehabilitation). The 25/50 rule was found to discourage rehabilitation of homes for two reasons. *Id.* First, it was discouraged because local inspectors' discretion over the smaller rehabilitation projects "made it difficult for contactors to make accurate estimates of rehabilitation costs." *Id.* Second, selective demolition and rehabilitation was costly, so "a project that exceeded the 50 percent threshold commonly ended up being far more expensive than constructing a new building from scratch." *Id.*

250. GEN. BUS. §§ 777–777-b.

Currently, the definition states that a builder is "any person, corporation, partnership or other entity contracting with an owner for the construction or sale of a new home."[251] Although this definition technically includes flippers, the inclusion of more specific language geared specifically towards these house flippers will remove any uncertainty about whether or not this warranty applies to the house-flipping market.[252]

V. CONCLUSION

While New York's statutory warranty for new home construction was a great stride away from the harsh doctrine of caveat emptor towards meaningful protections for home buyers, it is simply incomplete.[253] The Statute's attempts to even the playing field for buyers and sellers, and reconcile the legal inconsistencies of personal property and real property, failed to take into consideration a growing market of professional house flippers.[254] This growing market encourages sellers to cut corners and, in turn, puts the buyer at great risk for physical and economic harm—greater than the risks a buyer would face in an ordinary real estate transaction.[255] Without a change to New York's statutory warranty, buyers of new home construction will continue to be at the mercy of their sellers.[256]

The proposed amendment to Article 36-B would create a two-part test.[257] To determine coverage under this warranty system, the buyer would first need to see if their newly purchased home is considered "new home" construction.[258] After the buyer assesses that their home is considered new construction, they would look to the 25/50 rule to see how much, or which parts, of their home are protected by New York's statutory warranties that extend over a total of six years.[259] This two-part test will create clarity and a more concrete rule for buyers and sellers that will allow for predictability in the law.[260] In addition, shifting the assessment for which types of homes are deserving of these warranties to focus on the substantiality of the renovation will help to create a more

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251. *See* GEN. BUS. §§ 777–777-b.
252. GEN. BUS. §§ 777–777-b; Hendricks, *supra* note 18.
253. *See* GEN. BUS. § 777.
254. McDonald v. Mianecki, 398 A.2d 1283, 1288 (N.J. 1979).
255. Caceci v. Di Canio Constr. Corp., 526 N.E.2d 266, 269 (N.Y. 1988).
256. DeRoche v. Dame, 430 N.Y.S.2d 390, 392 (App. Div. 1980); Losito, *supra* note 83, at 375.
257. *See supra* Part IV.
258. *See* GEN. BUS. § 777.
259. ELLICKSON ET AL., *supra* note 228, at 472.
260. *See supra* Part IV.

fair system of accountability that may encourage professional builders to produce better-quality projects.[261]

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261. *See supra* Part IV.

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