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THE INSTALLMENT LAND CONTRACT AS LEASE: HABITABILITY PROTECTIONS AND THE LOW-INCOME PURCHASER

ERIC T. FREYFOGLE*

A purchaser who buys a home on an installment contract basis is often in exactly the same position as a tenant with a lease. There is, however, an important difference between lessee and purchaser: while a lessee is typically protected by an implied warranty of habitability, requiring landlords to put the premises in a habitable condition at the beginning of the lease and to maintain that condition throughout its term, an installment purchaser has no such protection. Professor Freyfogle persuasively argues that the implied warranty of habitability should extend to an installment contract sale when it is functionally equivalent to a lease. Such a functional equivalence test would focus on the purchaser's equity in the property, the similarity between the purchaser's payments and the rental value of the property, and the likelihood that the purchaser will default and the vendor will recover the property. If an installment sale satisfies this test, Professor Freyfogle argues, the purchaser should be entitled to the same protection granted to tenants, including an unwaivable implied warranty of habitability and the imposition of a landlord's tort duties and liabilities. Such an extension of the implied warranty, Professor Freyfogle concludes, will aid purchasers, who are generally low-income families, by extending to them the protections they deserve.

INTRODUCTION

The aim of this Article is simple: to suggest that, in certain, defined circumstances, courts should look beyond the form of a residential installment land contract and construe the transaction as a lease. When these circumstances are present and a court recasts a sale transaction as a lease, the court should impose on the vendor-landlord the same obligations that residential landlords have—to maintain the leased premises in habitable condition. This Article explains when and why courts should do this.

Over the past two decades courts in nearly all states have shown a marked willingness to disregard the free contract aspects of residential leases and to impose important obligations on landlords without regard to the intentions of the parties.¹ The most dramatic and burdensome of

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¹ For discussions of obligations imposed on landlords, see, e.g., Abbott, *Housing Policy, Housing Codes and Tenant Remedies: An Integration*, 56 B.U.L. Rev. 1, 4-66 (1976) (discussing development of implied warranty of habitability and housing codes); Chase & Taylor, *Landlord and Tenant: A Study in Property and Contract*, 30 Vill. L. Rev. 571, 641-88 (1985) (discussing limited development of implied warranty of habitability and failure of courts to accept, as an implied term, landlord's obligation to deal in good faith); Cunningham, *The New Implied and Statutory Warranties of Habitability in Residential Leases: From Contract to*

these obligations has been the obligation to put the leased premises in habitable condition at the beginning of the lease and to keep them habitable thereafter. This implied "warranty" of habitability is imposed not to fill in a gap in an incomplete lease but to further public policies favoring the maintenance of clean, safe housing.² The warranty therefore is generally not waivable by the parties.³

In similar fashion, courts have recently shown a willingness to ignore the free contract aspects of an installment land contract,⁴ a financ-

Status, 16 Urb. L. Ann. 3, 74-126 (1979) (discussing implied warranty of habitability and illegal contract approaches); Glendon, *The Transformation of American Landlord-Tenant Law*, 23 B.C.L. Rev. 503, 528-45 (1982) (discussing developments in landlord obligations and tort liability, tenant remedies, summary process cases, and lease terminations); Hicks, *The Contractual Nature of Real Property Leases*, 24 Baylor L. Rev. 443, 489-536 (1972) (discussing implied warranty of quality and doctrines of anticipatory breach, mitigation of damages, impossibility of performance, and frustration of purpose); Humbach, *The Common-Law Conception of Leasing: Mitigation, Habitability, and Dependence of Covenants*, 60 Wash. U.L.Q. 1213, 1261-87 (1983) (assessing conveyance and contract theories of leasing and their implications for reform).

² Mallor, *The Implied Warranty of Habitability and the "Non-Merchant" Landlord*, 22 Duq. L. Rev. 637, 646 (1984).

³ R. Cunningham, W. Stoebuck & D. Whitman, *The Law of Property* § 6.40 (1984); see text accompanying notes 66-76 *infra*.

⁴ See, e.g., *Curry v. Tucker*, 616 P.2d 8, 13 (Alaska 1980) (dictum) (court may, on equitable grounds, refuse to enforce a forfeiture provision in land sale contract where adequate compensation is available); *Hatfield v. Mixon Realty Co.*, 269 Ark. 803, 807-08, 601 S.W.2d 894, 897 (1980) (court may refuse to enforce forfeiture provision under "substantial equitable circumstance[s]"); *Petersen v. Hartell*, 40 Cal.3d 102, 109-10, 707 P.2d 232, 236, 219 Cal. Rptr. 170, 174-75 (1985) (court may refuse forfeiture and award specific performance, even to willfully defaulting purchaser); *McNorton v. Pan Am. Bank*, 387 So.2d 393, 396-97 (Fla. Dist. Ct. App. 1980) (court may ignore forfeiture clause and award defaulting purchaser restitution based on unjust enrichment); *Scholwin v. Johnson*, 147 Ill. App. 3d 598, 605-06, 498 N.E.2d 249, 254-55 (1986) (court may refuse to enforce forfeiture clause when purchaser has made substantial improvements to the property); *Skendzel v. Marshall*, 261 Ind. 226, 240-41, 301 N.E.2d 641, 650 (1973) (court may not enforce forfeiture clause when vendee has acquired substantial interest in property, but court may order foreclosure), cert. denied, 415 U.S. 921 (1974); *Sebastian v. Floyd*, 585 S.W.2d 381, 383 (Ky. 1979) (treating contracts as mortgages and requiring foreclosure in all cases); *Farmer v. Groves*, 276 Or. 563, 567, 555 P.2d 1252, 1255 (1976) (notice required to declare forfeiture, even when contract makes no provision for it, and notice period must be longer when vendor has waived his right to insist on prompt payment).

The most current examination of installment land contract law is my survey, "Installment Land Contracts," in 7 *Powell on Real Property* ¶¶ 938.20 to .26 (P. Rohan ed. 1987) [hereinafter *Powell*]; see also G. Nelson & D. Whitman, *Real Estate Finance Law* § 3.29 (2d ed. 1985) (discussing various approaches courts use to save purchasers from inequitable forfeiture clauses); Note, *Installment Land Contracts: The Illinois Experience and the Difficulties of Incremental Judicial Reform*, 1986 U. Ill. L. Rev. 91, 101-115 (arguing that judicial efforts in Illinois to diminish inequity of forfeiture have sacrificed desirable features of installment contracts without adequately protecting purchasers).

For suggestions on how to reform the treatment of installment land contracts, see *Mixon, Installment Land Contracts: A Study of Low Income Transactions, With Proposals for Reform and a New Program to Provide Home Ownership in the Inner City*, 7 *Hous. L. Rev.* 523, 554-619 (1970).

ing arrangement by which a purchaser takes possession immediately but, typically, receives title only when he has made all the periodic payments.⁵ Courts have ignored installment contract terms largely to protect purchasers from the possibly harsh consequences of forfeiture.⁶ When forfeiture occurs, purchasers can lose their property as well as the payments they have made on their contracts. Courts have attacked forfeiture clauses with vigor, most often by granting to purchasers some or all of the protections enjoyed by mortgagors under state mortgage law:⁷ the rights to reinstate contracts after default,⁸ to redeem property,⁹ to seek restitution of excess payments,¹⁰ and, in some cases, even to demand foreclosure.¹¹ By granting these rights, courts have, in effect, viewed the installment land contract as functionally similar to a mortgage. By drawing upon mortgage law, they have applied a body of law that aids the homeowner who has substantial equity in his home and who stands to lose the most upon default.

This transformation of installment land contract law, however, has done little for the low-equity purchaser under an installment contract. Low-equity purchasers need protection of a different sort; their concern is not equity protection but clean, safe, livable housing. In some parts of the country, property owners are selling dilapidated housing on installment contracts with financial terms indistinguishable from leases.¹²

⁵ G. Nelson & D. Whitman, *supra* note 4, § 3.26. During the contract period, the purchaser is normally required to pay taxes, maintain casualty insurance, and keep the premises in good repair. *Id.*

⁶ See 7 Powell, *supra* note 4, ¶ 938.20[3].

⁷ See *id.* ¶¶ 938.20[3], 938.22[6], 938.23[3]-.23[4].

⁸ See, e.g., *Parrott v. Heller*, 171 Mont. 212, 214-15, 557 P.2d 819, 820 (1976) (relying on general statutory policy against unfair forfeitures); *Shervold v. Schmidt*, 359 N.W.2d 361, 363-64 (N.D. 1984) (relying on waiver theory); *Phair v. Walker*, 48 Or. App. 641, 645-46, 617 P.2d 616, 619 (1980) (allowing purchaser to reinstate during required notice period before forfeiture); *Call v. Timber Lakes Corp.*, 567 P.2d 1108, 1109 (Utah 1977) (allowing purchaser to reinstate if forfeiture provision gives seller unconscionable benefit).

⁹ See, e.g., *Curry v. Tucker*, 616 P.2d 8, 13 (Alaska 1980) (in appropriate case court may set aside forfeiture so that purchaser can pay debt); *Petersen v. Hartell*, 40 Cal.3d 102, 109-10, 707 P.2d 232, 237, 219 Cal. Rptr. 170, 174-75 (1985) (allowing breaching purchaser to obtain specific performance); *Jenkins v. Wise*, 58 Haw. 592, 597, 574 P.2d 1337, 1341 (1978) (same); *Martinez v. Martinez*, 101 N.M. 88, 92-93, 678 P.2d 1163, 1167-68 (1984) (requiring notice period for forfeiture, during which purchaser can redeem); see also 7 Powell, *supra* note 4, ¶ 938.23[3] (discussing ways states create redemption rights).

¹⁰ See, e.g., *Honey v. Henry's Franchise Leasing Corp. of Am.*, 64 Cal.2d 801, 803, 415 P.2d 833, 834, 52 Cal. Rptr. 18, 19 (1966); *Jenkins v. Wise*, 58 Haw. 592, 598, 574 P.2d 1337, 1341 (1978); *Huckins v. Ritter*, 99 N.M. 560, 562, 661 P.2d 52, 54 (1983); *Heikkila v. Carver*, 378 N.W.2d 214, 219 (S.D. 1985).

¹¹ See, e.g., *Skendzel v. Marshall*, 261 Ind. 226, 240-41, 301 N.E.2d 641, 650, cert. denied, 415 U.S. 921 (1974); *Sebastian v. Floyd*, 585 S.W.2d 381, 383 (Ky. 1979).

¹² One series of articles claims, for example, that the installment land contract is replacing the lease as the most common arrangement for low-income housing in East St. Louis, Illinois. See, e.g., Kaplan, *Bond for Deed: Practice Called Solution and Problem for Poor Seeking*

They often do so with the reasonable expectation of recovering the property upon default and reselling the property to a new family, much as a landlord re-leases to a new tenant. As sellers rather than landlords, they can shift repair duties to the home residents and can profit from substandard housing—all in contravention of the public policies underlying the warranty of habitability.¹³ Although the scope of this problem is hard to assess, isolated reports suggest that “slumlords” in some areas are now selling rather than leasing because of the benefits of the installment land contract form.¹⁴ The “purchasers” to whom they sell have little if any real equity in their homes, pay monthly amounts identical to rent, and, like tenants, expect to lose their homes (and all their payments) if they miss a few monthly payments.¹⁵

This Article considers how courts should deal with the low-equity purchaser's need for protection. Part I examines the policy behind the implied warranty of habitability and considers some of the major issues courts have faced in defining it. Part II then describes how courts have reshaped installment land contracts. Together, recent decisions on the habitability warranty and installment land contracts strongly support the development of a new doctrine that would impose landlord duties on an installment land vendor who sells on a contract that is the functional equivalent of a residential lease.

Part III proposes a test for determining when a contract is the functional equivalent of a lease. It explains the merits and applications of the test and considers possible objections to it. The Article recommends that courts engage once again in a clear act of judicial lawmaking by applying the functional equivalence test. But, as the Article explains, the proposed “new” doctrine follows quite logically from other recent developments that have enjoyed wide currency and acceptability. It is, then, neither as new nor as revolutionary as it may at first appear.

The typical beneficiary of the new rule will be a family of modest means that is suffering great hardship because of a contract that arose

Homes, Belleville (Ill.) News-Democrat, July 27, 1986, § B, at 1, 3 [hereinafter Kaplan, Bond for Deed]. Predictably, housing conditions have continued to decline markedly because vendors deny all repair duties and tenants are unable to afford them. See Kaplan, Buyers Claim They Didn't Realize Terms of Contract, Belleville (Ill.) News-Democrat, July 27, 1986, § B, at 1, 3. Homes are sold with very low down payments. *Id.* Purchasers commonly misunderstand the contracts they sign and are surprised when they learn that they must make their own repairs and pay their own taxes. *Id.* Low-income residents have difficulties finding rental housing of any type. Homes for sale on contract, however, are plentiful because vendors regularly recover a property upon a purchaser default. See Kaplan, Bond for Deed, *supra*, at 1. The vendors then resell the property without making any significant repairs. Kaplan, Owners Blame Tenants for Slums, Belleville (Ill.) News-Democrat, July 27, 1986, § B, at 1.

¹³ See notes 17-36 and accompanying text *infra*.

¹⁴ See note 12 and accompanying text *supra*.

¹⁵ See *id.*

out of an unfair, poorly understood bargaining process. At issue is the vital resource of decent housing. The doctrine proposed here would make the law more fair and responsive as well as more consistent.

I

THE LOGIC OF THE IMPLIED WARRANTY OF HABITABILITY

In the 1960s and 1970s nearly all states imposed on landlords an obligation to maintain the habitability of leased premises.¹⁶ One of many reasons for the adoption of this obligation¹⁷ was that economic changes had rendered the old rule of *caveat emptor* inappropriate. *Caveat emptor* required lessees to inspect property before leasing and to make all needed repairs. The doctrine arose out of an agrarian economy in which landlords and tenants typically had equal skills in inspecting and repairing property.¹⁸ Because leases largely covered farmland, the value of the structures on the land was of secondary importance.¹⁹ In the opinion of early courts, a lease was viewed most accurately as a conveyance of property from one party to another.²⁰ Today, by contrast, a residential lease typically involves a bundle of goods and services and envisions a continuing relationship between the landlord and tenant. For the typical tenant, the apartment or house being leased is far more important than the land.²¹

A second reason for the new warranty was the typical inequality in bargaining positions of the landlord and tenant.²² With inequality came the prospect of overreaching and unfair terms, and courts looked with particular suspicion on lease terms that imposed on tenants full duties to inspect and repair.²³ In the view of many, the law needed to respond to this inequality and restore the parties to a reasonable balance.²⁴

¹⁶ See Mallor, *supra* note 2, at 637 n.3 (listing "at least forty jurisdictions" imposing implied warranty of habitability on landlords as of 1984); see also R. Cunningham, W. Stoebuck & D. Whitman, *supra* note 3, §§ 6.38 to .39; R. Schoshinski, *American Law of Landlord and Tenant* § 3:16 (Supp. 1986).

¹⁷ See Mallor, *supra* note 2, at 642-46 (discussing reasons for development of new warranty); authorities cited in note 1 *supra* (same).

¹⁸ See Mallor, *supra* note 2, at 642-43.

¹⁹ *Id.* at 643.

²⁰ See *Javins v. First Nat'l Realty Corp.*, 428 F.2d 1071, 1074 (D.C. Cir.), cert. denied, 400 U.S. 925 (1970); *Helton v. Reynolds*, 640 S.W.2d 5, 8 (Tenn. Ct. App. 1982); Weinberg, *From Contract to Conveyance: The Law of Landlord and Tenant, 1800-1920* (pt. 1), 1980 S. Ill. U.L.J. 29, 32-38; see also H. Lesar, *The Landlord-Tenant Relation in Perspective: From Status to Contract and Back in 900 Years?*, 9 U. Kan. L. Rev. 369, 372-75 (1961).

²¹ See, e.g., *Javins*, 428 F.2d at 1077-79.

²² Mallor, *supra* note 2, at 644.

²³ See *id.*

²⁴ See, e.g., *Javins*, 428 F.2d at 1079; *Green v. Superior Court*, 10 Cal.3d 616, 624, 517 P.2d 1168, 1173-74, 111 Cal. Rptr. 704, 709 (1974); *Mease v. Fox*, 200 N.W.2d 791, 794-95

A third reason underlying the development of the implied warranty of habitability was that landlords were usually better positioned to make needed repairs.²⁵ In multi-unit structures, tenants often had no access to the central elements of the building such as water, electrical, heating, and cooling systems.²⁶ Even if they did have access, tenants often lacked the expertise necessary to make repairs.²⁷ As short-term leases became the norm, tenants had insufficient financial incentive to make major structural repairs even if they possessed the resources to undertake the repairs.²⁸ Landlords, in contrast, had long-term stakes in property; their superior knowledge, access, and skill, coupled with greater financial interest, made the imposition of a duty to repair fair and reasonable.²⁹

Tenant expectations also played an important role in the new warranty of habitability.³⁰ As the social and economic contexts of residential leases changed, so did the expectations of the typical tenant. Tenants leased homes, and they expected to be able to move into their homes without undue trouble or expense. They expected toilets to flush and furnaces to heat. To an increasing extent, they leased appliances as well as space, and they expected the appliances to function properly. Repairs with a long useful life, they believed, were the proper province of the landlord. Just as the tenant had an obligation to pay rent every month, the landlord had a continuing obligation to provide good shelter month by month.³¹ These shifting expectations, as often is the case, outpaced legal reforms. But by the 1960s and 1970s, courts accepted these expectations as valid and undertook to protect them.³²

Perhaps the prime motive behind the new habitability duty, however, was the public policy concern over the quality of the nation's housing stock.³³ Dilapidated housing was a public as well as a private

(Iowa 1972); *King v. Moorehead*, 495 S.W.2d 65, 69-71 (Mo. Ct. App. 1973).

²⁵ *Mallor*, supra note 2, at 645.

²⁶ *Id.*

²⁷ *Id.* at 643-44.

²⁸ *Id.* at 645-46.

²⁹ *Id.*

³⁰ *Id.* at 645.

³¹ See *Javins v. First Nat'l Realty Corp.*, 428 F.2d 1071, 1077-79 (D.C. Cir.), cert. denied, 400 U.S. 925 (1970).

³² See, e.g., *id.*; *Jack Spring, Inc. v. Little*, 50 Ill. 2d 351, 362-66, 280 N.E.2d 208, 215-17 (1972).

³³ See, e.g., *Javins*, 428 F.2d at 1079-80 ("[P]oor housing is detrimental to the whole society, not merely to the unlucky ones who must suffer the daily indignity of living in a slum."); *Pines v. Persson*, 14 Wis. 2d 590, 595-96, 111 N.W.2d 409, 412-13 (1961) (stating that need for and social desirability of adequate housing in era of rapidly increasing population require imposition of implied warranty of habitability).

Professor Kronman has articulated this public policy concern as an issue of distributive fairness. See *Kronman, Paternalism and the Law of Contracts*, 92 *Yale L.J.* 763, 766-74 (1983) [hereinafter *Kronman, Paternalism*] (using prohibition against waiver of implied war-

concern. Substandard housing created filth that spread to the streets. It bred disease if not crime. It was an eyesore and a public disgrace, and it created discomfort and distress for the poor who had to live in it.³⁴ Housing codes attempted to address this problem, but their enforcement was dramatically inadequate.³⁵ Private enforcement seemed necessary, and the new habitability duty seemed to be a useful enforcement tool.³⁶

The warranty of habitability gained prominence in the 1960s but had respectable origins from a much earlier period. Louisiana, California, and other states with a civil law heritage had long imposed repair duties on landlords.³⁷ Moreover, a few western states adopted versions of David Dudley Field's Civil Code, which imposed on a lessor a duty to maintain leased dwellings in habitable condition.³⁸ Often these duties could be waived by contract,³⁹ but they provided a useful first step. In *Pines v. Persson*,⁴⁰ the Wisconsin Supreme Court initiated a wave of reform by holding that landlords implicitly warranted the habitability of their premises at the commencement of a lease.⁴¹ Judge Skelly Wright carried the idea a major step forward in *Javins v. First National Realty Corp.*,⁴² by extending the habitability warranty from the beginning of the lease throughout the entire term.⁴³ Judge Wright's use of the term "warranty" to refer to a continuing obligation was inaccurate and misleading. A warranty is a legally binding representation that a particular state of

ranty of habitability as example of "paternalism" that can be defended in economic terms). Professor Kronman asserts that the warranty redistributes power over housing from landlords to tenants. Redistribution of housing resources makes sense because society values the fair distribution of housing resources while it is indifferent to the distribution of many other resources, such as (to use his example) expensive paintings. *Id.* at 771. On the larger question of using contract law for the purpose of wealth redistribution, see Kronman, *Contract Law and Distributive Justice*, 89 *Yale L.J.* 472, 475 (1980) (arguing that although any redistributive scheme will lead to conflict between distributive justice and individual liberty, there is still no persuasive reason to adopt nondistributive conception of contract law); Michelman, *Norms and Normativity in the Economic Theory of Law*, 62 *Minn. L. Rev.* 1015, 1016-37 (1978) (using housing law to illustrate that normative, rather than positive or economic, interpretations of law are to be preferred).

³⁴ See, e.g., *Berman v. Parker*, 348 U.S. 26, 32-33 (1954) ("Miserable and disreputable housing conditions may do more than spread disease and immorality. They may also suffocate the spirit by reducing the people who live there to the status of cattle.").

³⁵ See Cunningham, *supra* note 1, at 10-51 (describing in detail use of housing codes to upgrade poor housing).

³⁶ See *Javins*, 428 F.2d at 1080-82; *Pines*, 14 Wis. 2d at 595-96, 111 N.W.2d at 412-13.

³⁷ See R. Cunningham, W. Stoebuck & D. Whitman, *supra* note 3, § 6.39, at 321.

³⁸ *Id.* at 321-22.

³⁹ See Cunningham, *supra* note 1, at 57.

⁴⁰ 14 Wis. 2d 590, 111 N.W.2d 409 (1961).

⁴¹ *Id.* at 595-96, 111 N.W.2d at 412-13.

⁴² 428 F.2d 1071 (D.C. Cir.), cert. denied, 400 U.S. 925 (1970); see Glendon, *supra* note 1, at 525-26.

⁴³ *Javins*, 428 F.2d at 1079-82.

facts is true.⁴⁴ What *Javins* actually imposed on landlords was a covenant—a promise to make necessary repairs when needed.⁴⁵ It required landlords to provide not a factual representation but a continuing, burdensome service. In *Pines*, by contrast, the court used the term properly when it required that the landlord warrant that the leased premises as a factual matter were habitable on the first day of a lease.⁴⁶

In the years after *Pines* and *Javins*, courts attempted to shape the habitability warranty. In so doing, they faced the difficult task of defining “habitable.”⁴⁷ *Javins* concerned an urban apartment covered by a housing code, and the opinion thus defined habitability in terms of compliance with that code.⁴⁸ *Javins* ostensibly required full compliance but included dictum that “one or two minor violations standing alone which do not affect habitability are *de minimis*.”⁴⁹ Other jurisdictions took a similar route and required substantial compliance with the applicable code.⁵⁰ When codes were lacking, however, courts faced greater difficulties, and the articulation of a working definition of habitability remains an elusive goal.

The Illinois Supreme Court attempted to define “habitable” in 1985 in *Glase v. Trinkle*,⁵¹ holding that the habitability warranty applied to homes not covered by any housing code.⁵² In resolving this issue, the court set forth one of the best expressions of habitability to date. The court acknowledged that housing standards may vary as community standards vary, and that the type of property and the amount of rent

⁴⁴ A warranty is a “promise that a proposition of fact is true.” Black’s Law Dictionary 1423 (5th ed. 1979). In other words, it is an affirmative statement by a party to a contract that he will be liable if a particular set of facts proves to be untrue.

⁴⁵ See *Jack Spring, Inc. v. Little*, 50 Ill.2d 351, 373, 280 N.E.2d 208, 220 (1972) (Ryan, J., dissenting). In contrast to a warranty, a covenant is a contractual promise, or an “agreement, convention, or promise of two or more parties, by deed in writing, signed, and delivered, by which either of the parties pledges himself to the other that something is either done, or shall be done, or shall not be done, or stipulates for the truth of certain facts.” Black’s Law Dictionary 327 (5th ed. 1979). Logically, a landlord could warrant that leased premises would always be habitable. If they ceased to be habitable, the warranty would be breached, even if the landlord had no notice or chance to cure. If the landlord covenanted to keep leased premises in repair, on the other hand, he would be liable only if he failed to make repairs, presumably within a reasonable time. A covenanting landlord, therefore, would be entitled to notice of a defect and a chance to cure it.

⁴⁶ See 14 Wis. 2d 590, 596, 111 N.W.2d 409, 412-13 (1961).

⁴⁷ See R. Cunningham, W. Stoebuck & D. Whitman, *supra* note 3, at 315-18 (describing varying state court interpretations of “habitable”); Chase & Taylor, *supra* note 1, at 646-65 (describing broad and narrow judicial readings of *Javins*).

⁴⁸ See *Javins*, 428 F.2d at 1072.

⁴⁹ *Id.* at 1082 n.63.

⁵⁰ See Cunningham, *supra* note 1, at 83-84 (discussing extent to which “habitable” should be defined by applicable housing code).

⁵¹ 107 Ill. 2d 1, 479 N.E.2d 915 (1985).

⁵² *Id.* at 10, 479 N.E.2d at 918-19.

paid limit a tenant's legitimate expectations.⁵³ Nonetheless, the court continued, the warranty of habitability imposes certain minimum requirements: that a dwelling be fit for its intended use; that, at the inception of the lease, the dwelling be free from latent defects in facilities essential to occupancy; and that the premises remain habitable throughout the lease term.⁵⁴ Breach of the implied warranty occurs when a defect is so substantial that it renders the dwelling unsafe or unsanitary and thus unfit for occupancy.⁵⁵ In determining whether a defect constitutes a breach of the warranty, courts should consider a number of factors, including the nature of the deficiency and its effect on habitability, the age and location of the building, the rent paid, waiver by the tenant, and the tenant's contribution to the defect through abnormal or unusual use.⁵⁶ A low-rent tenant in a well-worn home, therefore, cannot expect the same level of services as the tenant of a new, expensive home. Nevertheless, certain expectations are properly held by all people, and the implied warranty provides a minimum standard below which rental housing cannot fall.

In addition to defining "habitable," courts also had to define the scope of the implied warranty of habitability. Does it apply to all types of rental housing or only to multi-unit housing or housing leased by merchant landlords?⁵⁷ Most courts have noted that the rationales for the implied warranty apply to leases of single-family homes by nonprofessional landlords and have extended the warranty to cover such leases.⁵⁸ The issue has caused some hesitation, however, largely because the imposition of tort liability seems to follow naturally whenever the landlord "warrants" that the leased premises will always be habitable and the warranty later proves false.⁵⁹ If a defect affecting habitability causes injury, a true "warranty" would be breached, and the landlord would be liable without any showing of negligence. Although this result makes sense in the case of merchant landlords, it has seemed unjust for others. Courts

⁵³ See *id.* at 12, 479 N.E.2d at 919.

⁵⁴ *Id.* at 13, 479 N.E.2d at 919-20.

⁵⁵ *Id.* at 13, 479 N.E.2d at 920.

⁵⁶ *Id.* at 14, 479 N.E.2d at 920.

⁵⁷ See Cunningham, *supra* note 1, at 81-83; Mallor, *supra* note 2, at 638-40, 654-68.

⁵⁸ See, e.g., Pole Realty Co. v. Sorrells, 84 Ill. 2d 178, 182-83, 417 N.E.2d 1297, 1300 (1981) (citing decisions from various jurisdictions supporting implied warranty of habitability for leases of single-family dwellings). The implied warranty of habitability has been applied in somewhat different form to sales of new homes. In that setting, courts have also considered whether to apply the warranty to homes built and sold by small-time or occasional builders. Most courts have yet to address the issue, but the sense to date is that the warranty should apply. See, e.g., Park v. Sohn, 89 Ill. 2d 453, 461-63, 433 N.E.2d 651, 655-56 (1982) (applying warranty even though builder lived in home prior to sale and had built only one other home).

⁵⁹ See Browder, The Taming of a Duty—The Tort Liability of Landlords, 81 Mich. L. Rev. 99, 118-22 (1982) (discussing cases imposing strict liability on landlords).

have been reluctant to impose burdensome tort liability on landlords with only one or a few rental units, particularly liability that seems close to strict liability,⁶⁰ and a few courts have expressed reservations about extracting a warranty from these nonmerchants.⁶¹

Gradually, however, courts are realizing that the implied warranty is actually a covenant rather than a warranty, which means that breaches need not give rise to excessive tort liability.⁶² The landlord's repair covenant is (or at least should be) breached only if the landlord fails to fix a problem within a reasonable period after notice.⁶³ It is the landlord's inaction—the landlord's negligence—that gives rise to liability. This type of liability can be placed as comfortably on the nonmerchant landlord as on the merchant landlord. Most jurisdictions have accepted this logic and have agreed that the habitability duty is borne equally by all landlords, regardless of property holdings.⁶⁴ They have also largely agreed that landlords are liable in tort only for negligence in their performance of repair duties.⁶⁵ With this tort liability, the warranty offers additional important benefits to tenant safety. Tort liability can heighten the safety consciousness of landlords and lead to reductions in home

⁶⁰ See *Asper v. Haffley*, 312 Pa. Super. 424, 431-32, 458 A.2d 1364, 1368-69 (1983); *Mallor*, supra note 2, at 650-61.

⁶¹ See, e.g., *Zimmerman v. Moore*, 441 N.E.2d 690, 695-96 (Ind. Ct. App. 1982); *Conroy v. 10 Brewster Ave. Corp.*, 97 N.J. Super. 75, 81-82, 234 A.2d 415, 418-19 (App. Div. 1967).

⁶² See notes 44-45 supra (comparing warranties and covenants).

⁶³ See *Browder*, supra note 59, at 118-41; *Mallor*, supra note 2, at 653-54.

⁶⁴ The Uniform Residential Landlord and Tenant Act imposes the warranty on all landlords, without regard to merchant status. See *Unif. Res. Landlord and Ten. Act* § 2.104, 7B U.L.A. 460 (1985). That Act has now been adopted by 14 states. 7B U.L.A. 24 (Supp. 1987). Many other states also have statutes that make no exception for nonmerchants. See, e.g., *Cal. Civ. Code* § 1941 (West 1985); *Conn. Gen. Stat. Ann.* § 47a-7 (West Supp. 1987); *Del. Code Ann. tit. 25, § 5303* (1975); *Md. Real Prop. Code Ann.* § 8-211 (1981); *N.Y. Real Prop. Law* § 235-b (McKinney Supp. 1987). The occasional limit on the warranty tends to be narrow. See, e.g., *Mass. Gen. Laws Ann. ch. 186, § 19* (West 1977) (warranty inapplicable to owner-occupied two or three family dwelling). One court has considered the issue directly and rejected the claimed exemption for nonmerchants. See *Boudreau v. General Elec. Co.*, 2 Haw. App. 10, 625 P.2d 384 (1982).

Many cases have applied the warranty to single-family homes. See, e.g., *Lemle v. Breeden*, 51 Haw. 426, 462 P.2d 470 (1969); *Pole Realty Co. v. Sorrells*, 84 Ill. 2d 178, 417 N.E.2d 1297 (1981); *Mease v. Fox*, 200 N.W.2d 791 (Iowa 1972); *Pines v. Perssion*, 14 Wis. 2d 590, 111 N.W.2d 409 (1961). Moreover, some of the cases relating to single-family homes have involved landlords who seem to have been nonmerchants. See, e.g., *Steele v. Latimer*, 214 Kan. 329, 521 P.2d 304 (1974); *Marini v. Ireland*, 56 N.J. 130, 265 A.2d 526 (1970); *Foisy v. Wyman*, 83 Wash. 2d 22, 515 P.2d 160 (1973). Finally, several leading decisions adopting the warranty state that the warranty applies to *all* residential leases. See, e.g., *Green v. Superior Court*, 10 Cal. 3d 616, 629, 517 P.2d 1168, 1176, 111 Cal. Rptr. 704, 712 (1974); *Mease*, 200 N.W.2d at 791; *Boston Hous. Auth. v. Hemingway*, 363 Mass. 184, 198-99, 293 N.E.2d 831, 842-43 (1973); *Berzito v. Gambino*, 63 N.J. 460, 470, 308 A.2d 17, 22 (1973); *Foisy*, 83 Wash. 2d at 22, 515 P.2d at 160.

⁶⁵ See *Browder*, supra note 59, at 122-41; *Davis & DeLaTorre*, *A Fresh Look at Premises Liability as Affected by the Warranty of Habitability*, 59 Wash. L. Rev. 141, 154-60 (1984).

accidents.

Courts and legislatures have also had to determine whether the parties to a lease should be able to waive the new implied warranty and shift repair duties back to tenants. Early on, *Javins v. First National Realty Corp.* took a firm stand against waiver.⁶⁶ In that court's view, inequality in landlord-tenant bargaining power created a need for the warranty.⁶⁷ That same inequality could easily lead to boilerplate lease clauses waiving the warranty, clauses that could become so routine as to leave prospective tenants with no option.⁶⁸ Routine private waivers would also undercut the public benefits that flow from clean, safe housing.⁶⁹

Other jurisdictions have largely agreed that waivers are contrary to public policy.⁷⁰ They have hesitated on this issue, however, in the case of the single-family home.⁷¹ The landlord of a single rental home will often possess no greater repair expertise and no greater bargaining power than the tenant. In light of this consideration, the Uniform Residential Landlord Tenant Act recommends that waiver be allowed on a single family home if the waiver is specific, is entered into in good faith, and is not for the purpose of evading the landlord's obligations.⁷² *The Restatement (Second) of Property* takes a similar stance, permitting parties to a lease for single-family occupancy to waive certain landlord obligations.⁷³ A number of cases have rejected the possibility of an effective tenant waiver of the implied warranty,⁷⁴ but no court has considered the validity of a bargained-for waiver in the context of a single-family home.⁷⁵ Logic strongly supports a qualified allowance. A waiver should not extend to major structural repairs or other substantial repairs with a long useful life.⁷⁶ Other repairs, however, are within the tenant's reach and, in the

⁶⁶ See 428 F.2d 1071, 1081-82 (D.C. Cir.), cert. denied, 400 U.S. 925 (1970).

⁶⁷ See id. at 1079.

⁶⁸ See id. at 1079, 1081-82.

⁶⁹ Id. at 1082.

⁷⁰ See, e.g., *Green v. Superior Court*, 10 Cal. 3d 616, 625 n.9, 517 P.2d 1168, 1173 n.9, 111 Cal. Rptr. 704, 709 n.9 (1974) ("[L]andlords generally [should] not be permitted to use their superior bargaining power to negate the warranty of habitability rule."); *Boston Hous. Auth. v. Hemingway*, 363 Mass. 184, 199, 293 N.E.2d 831, 843 (1973) ("This warranty (insofar as it is based on the State Sanitary Code and local health regulations) cannot be waived by any provision in the lease."); *Foisy v. Wyman*, 83 Wash. 2d 22, 28, 515 P.2d 160, 164 (1973) ("[T]his type of bargaining by the landlord with the tenant is contrary to public policy and the purpose of the doctrine of implied warranty."); cf. *Kronman, Paternalism*, supra note 33, at 766-74 (justifying nonwaiver rule in terms of economic efficiency).

⁷¹ See, e.g., Conn. Gen. Stat. Ann. § 47a-7(c) (West Supp. 1987); *R. Cunningham, W. Stoebeck & D. Whitman*, supra note 3, § 6.40, at 328-32.

⁷² *Unif. Res. Landlord and Ten. Act* § 2.104(c), 7B U.L.A. 460 (1985).

⁷³ *Restatement (Second) of Property, Landlord and Tenant* § 5.6 & comment e (1977).

⁷⁴ See notes 66-70 and accompanying text supra.

⁷⁵ See *R. Cunningham, W. Stoebeck & D. Whitman*, supra note 3, at 331.

⁷⁶ See *R. Schoshinski*, supra note 16, § 5:20, at 278 (noting that express covenants by ten-

case of a bargained-for waiver, could be imposed on tenants without upsetting their reasonable expectations.

In sum, as the new implied warranty has taken shape it has resisted all efforts to reduce its influence. It extends to areas lacking building codes and to all residences, even single-family homes; it has supported tort liability and has resisted landlords' efforts to waive it. Although evidence is hard to gather, it seems likely that the implied warranty has yielded many of its promised benefits in the form of safer, more comfortable housing. It has done so, moreover, without noticeable landlord resistance—perhaps an indication of its consistency with widely shared values and expectations. Based on the available evidence to date, the implied warranty has been a success. And it is a success properly credited to those courts that overlooked the received common law and constructed a new framework of rights and obligations that respond better to the realities of today's housing market.

II

TRANSFORMING THE INSTALLMENT LAND CONTRACT

Like the residential lease, the residential installment contract has undergone substantial change. Decades ago, vendors under installment contracts enjoyed a large degree of dominance.⁷⁷ Upon a purchaser's default, a vendor could declare a forfeiture, recover the property, and retain all payments made under the contract. For a purchaser with substantial equity in his property, the loss could be considerable. Today, however, many states are providing safeguards for the installment home buyer who has built up some equity in his property.

The installment contract form can be chosen by any agreeing vendor and purchaser. When interest rates are high, financing by the seller is more common and installment contracts are executed with greater frequency, even by purchasers with substantial money and knowledge.⁷⁸ Typically, however, residential installment contracts are executed by low-income purchasers who lack access to normal mortgage financing.⁷⁹ Although the quality of homes sold on contract can vary, they usually are inexpensive and poorly constructed, whether new or used.⁸⁰

The installment contract form is appealing for several reasons to

ants to "keep leased premises in repair" are usually limited to ordinary rather than structural repairs); text accompanying notes 25-29 *supra* (noting that landlords have access to major structural components of buildings and greater expertise and financial incentive than tenants to repair).

⁷⁷ See G. Nelson & D. Whitman, *supra* note 4, § 3.27.

⁷⁸ See 7 Powell, *supra* note 4, ¶ 938.20[2], at 84D-8.

⁷⁹ See, e.g., Mixon, *supra* note 4, at 525-26.

⁸⁰ See *id.* at 537-40.

purchasers with little equity to invest in a home. First, closing costs on an installment sale can be kept to a minimum. Purchasers can avoid paying for legal assistance, title reports, title insurance, and the appraisals and inspections that outside lenders usually demand. Most significant, purchasers need not pay the up-front fees or "points" that lenders often charge. Moreover, installment contracts typically offer the possibility of lower down payments. When a home is fairly priced, the relative ease and low expense of the forfeiture remedy can justify a low down payment. In many cases, however, vendors inflate sale prices a bit, aware that low-equity, often low-income, purchasers have few other purchase options and that no independent appraisal will reveal the amount of inflation.⁸¹ With prices inflated, vendors have an even greater ability to sell for little or no money down.

The typical installment contract home buyer has long appeared to courts as a poorly advised, poorly protected, often lower-income purchaser. These purchasers are typically ill-prepared to unravel the textual ambiguities and considerable risks of the installment contract and to undertake needed protective steps. Like tenants, installment contract home buyers frequently fail to obtain independent legal advice or independent advice of any sort.⁸² Because they do not obtain outside financing, they do not benefit from the precautions demanded by typical mortgage lenders: inspections, appraisals, title reports, termite certificates, and other evidence of a property's value.⁸³ Although lenders seek to protect their own interests, their demands for caution also benefit borrowers.

In a wave of paternalistic protection, courts have reshaped the law of installment contracts to protect these purchasers against loss.⁸⁴ In doing so they have focused entirely on forfeiture and the losses that follow from it,⁸⁵ and they have sought to elevate the installment purchaser to a status much like that of the mortgagor.⁸⁶

States have responded to the perceived inequities of forfeiture in several ways. Some states have come to view the installment land contract as the functional equivalent of a mortgage and have granted purchasers

⁸¹ There has never been a definitive study of this problem. But see *id.* at 542-43, 591-92 (considering the issue).

⁸² See *id.* at 536; Note, *supra* note 4, at 108; see also Eskridge, *One Hundred Years of Ineptitude: The Need for Mortgage Rules Consonant With the Economic and Psychological Dynamics of the Home Sale and Loan Transaction*, 70 *Va. L. Rev.* 1083, 1112-28 (1984) (discussing poor decision-making process employed by prospective home buyers and mortgagors and lack of meaningful data available to them).

⁸³ Note, *supra* note 4, at 108-09.

⁸⁴ See 7 Powell, *supra* note 4, ¶ 938.20[3].

⁸⁵ See *id.* ¶¶ 938.20[3], 938.22, 938.23, 938.24[2].

⁸⁶ See, e.g., *Skendzel v. Marshall*, 261 *Ind.* 226, 301 *N.E.2d* 641 (1973), cert. denied, 415 *U.S.* 921 (1974); *Sebastian v. Floyd*, 585 *S.W.2d* 381 (Ky. 1979); 7 Powell, *supra* note 4, ¶¶ 938.22[6], 938.23[1].

the full range of mortgagor protections.⁸⁷ Purchasers in these states have an equitable right of redemption⁸⁸ that the vendor can terminate only by foreclosure.⁸⁹ These purchasers presumably can take advantage of any rights of reinstatement and statutory rights of redemption that are extended to mortgagors and can claim any surplus from the foreclosure sale.⁹⁰

Treating an installment land contract as a mortgage is harsh because it largely destroys the installment contract as a unique financing alternative.⁹¹ If foreclosure is always required, the installment contract loses its special features.⁹² Consequently, vendors will not want to sell on contract to purchasers who fail to qualify for traditional mortgage financing. Some states have taken a less drastic route by transforming installment land contracts into mortgages only when the purchaser has developed substantial equity in the property.⁹³ In these states, the installment contract form is respected, and forfeiture is allowed until a certain equity level is reached or a specified time period has passed. At that point, the contract converts into a mortgage and the purchaser thereafter enjoys the

⁸⁷ G. Nelson & D. Whitman, *supra* note 4, § 3.29, at 92, 104-08; Note, *supra* note 4, at 110-11; see, e.g., *Sebastian*, 585 S.W.2d at 383 (treating installment land contract as mortgage and requiring judicial sale of property upon default); *Duke v. Werbalowksy*, 115 A.D.2d 947, 497 N.Y.S.2d 524 (1985) (granting vendee possession until equitable title is foreclosed); Md. Real Prop. Code Ann. §§ 10-101 to -108 (Supp. 1986) (treating contract as mortgage if contract covers residential property and purchaser is not corporation); Okla. Stat. Ann. tit. 16, § 11A (West 1986) (deeming all contracts for deed constructive mortgages subject to foreclosure).

⁸⁸ In the mortgage law context, an equitable right of redemption is a transferable property right. A purchaser who exercises this right and redeems must pay the entire outstanding balance on the property. Upon payment, the purchaser is entitled to a deed. 7 Powell, *supra* note 4, ¶ 938.23[3].

⁸⁹ See, e.g., *Sebastian*, 585 S.W.2d at 381; *Skendzel*, 261 Ind. at 234-42, 301 N.E.2d at 646-50.

⁹⁰ The precise rights of a purchaser in a foreclosure action have not been considered by appellate courts, but there is no reason to suspect that they will be greater or less than the rights of other mortgagors. See, e.g., *Arnold v. Melvin R. Hall, Inc.*, 496 N.E.2d 63, 66 (Ind. 1986) (applying normal mortgage law rules on deficiency judgments to foreclosure action brought by installment contract vendor).

⁹¹ See Note, *supra* note 4, at 110-11.

⁹² Briefly, the installment land contract, when enforced according to its terms, is attractive because vendors are willing to sell with less money down since they can recover the property quickly after a default and need not incur the time and expense of foreclosure; closing is expedited and less costly because no outside lender is involved, and inspections, credit checks, and surveys are not required; and stringent lender credit requirements are inapplicable, again because no outside lender is involved. This last factor aids both vendors and purchasers; it enables purchasers to buy when they otherwise could not, and it gives vendors a wider range of possible purchasers. See 7 Powell, *supra* note 4, ¶ 938.20[2], at 84D-6 to -7.

⁹³ Note, *supra* note 4, at 111. See, e.g., *Skendzel*, 261 Ind. at 226, 301 N.E.2d at 641; Mont. Code Ann. §§ 52-401 to -417 (Supp. 1975); Ohio Rev. Code Ann. §§ 5313.01-.10 (Baldwin 1986).

protections of mortgage law.⁹⁴ This convertibility option was adopted in a prominent Indiana decision⁹⁵ and enjoys widespread support today among commentators.⁹⁶

Other states, by judicial and legislative action, have developed protections designed specifically for installment purchasers.⁹⁷ In general, these protections are weaker than mortgage law protections but similar in form. Several states give purchasers a type of equitable right of redemption by delaying forfeiture while the purchaser attempts to arrange refinancing.⁹⁸ In some states, courts claim the equitable power to delay forfeiture as justice demands or to condition it so as to achieve a fair result.⁹⁹ Other states grant a right of reinstatement, which enables the purchaser to keep the property by paying just the overdue installments rather than the entire unpaid balance.¹⁰⁰

Some states have chosen a more cautious, less effective route in protecting installment contract purchasers. Still, their actions have displayed the same willingness to ignore contract forms in search of a fair result. Illinois courts, for example, have developed a series of legal doctrines that they employ to soften the harshness of forfeiture.¹⁰¹ They often find that a vendor's acceptance of late payments in the past constitutes a waiver of his right to declare a forfeiture for subsequent late pay-

⁹⁴ See, e.g., Ill. Ann. Stat. ch. 110, para. 15-1106(2) (Smith-Hurd Supp. 1987); Ohio Rev. Code Ann. § 5313.07 (Baldwin 1986); 7 Powell, *supra* note 4, ¶ 938.22[6], at 84D-61 to -65.

⁹⁵ Skendzel v. Marshall, 261 Ind. 226, 301 N.E.2d 641 (1973), cert. denied, 415 U.S. 921 (1974).

⁹⁶ See, e.g., Power, Land Contracts as Security Devices, 12 Wayne L. Rev. 391, 432-33 (1966) (proposing statutory protections for high-equity purchasers); Note, Reforming the Vendor's Remedies for Breach of Installment Land Sale Contracts, 47 S. Cal. L. Rev. 191, 216-23 (1973) (stating that authorities generally agree that an installment land sale contract operates as an "equitable conversion"); Note, *supra* note 4, at 112 (noting that many writers favor convertibility approach but disagree on percentage of purchase price that purchaser should have to pay to convert land contract to mortgage).

⁹⁷ See G. Nelson & D. Whitman, *supra* note 4, § 3.29, at 93-103 (discussing statutory and judicial limitations on forfeiture); see also Note, *supra* note 4, at 101-08 (discussing Illinois's legislative and judicial provisions that protect installment purchasers).

⁹⁸ States create redemption rights in several ways. A few states create express redemption rights by statute. More states create a redemption period by requiring a vendor to give notice of a possible forfeiture and allowing the purchaser to redeem during that period. Other states create a redemption right by granting to purchasers the right to seek specific performance of the contract when they are in default. Finally, some states simply place equitable limits on the enforceability of forfeiture clauses, which allows courts to permit redemption when equity seems to require it. See 7 Powell, *supra* note 4, ¶ 938.23[3] (discussing various redemption methods in detail).

⁹⁹ See *id.* ¶ 938.23[3], at 84D-80 to -81.

¹⁰⁰ See, e.g., Iowa Code Ann. § 656.2 (West Supp. 1987); N.D. Cent. Code § 32-18-04 (1976); Ohio Rev. Code Ann. § 5313.05 (Baldwin 1986); Wash. Rev. Code Ann. § 61.30.090 (Supp. 1987).

¹⁰¹ See 7 Powell, *supra* note 4, ¶ 938.23[5]; Note, *supra* note 4, at 101-08.

ments.¹⁰² The vendor can reinstate the right, but only by giving the purchaser notice of his intent to require timely payments in the future.¹⁰³ In addition, Illinois courts may require perfect compliance with any contract provision setting out a procedure for declaring forfeiture and seize upon minor errors to delay a forfeiture.¹⁰⁴ Like other states, Illinois also employs the election of remedies doctrine, which requires a vendor who declares a forfeiture and recovers property to give up any right to a deficiency judgment.¹⁰⁵ The election of remedies doctrine operates much like mortgage law antideficiency rules, which bar a mortgagee from seeking a deficiency judgment against a debtor-mortgagor if the mortgage foreclosure sale proceeds fail to cover all amounts due on a mortgage.¹⁰⁶ Finally, Illinois courts have exercised some equitable discretion to delay forfeiture while the purchaser seeks to refinance and cure the default.¹⁰⁷

Elsewhere, courts have exercised equitable discretion by conditioning forfeiture on the vendor's restitution to the purchaser of purchase payments that exceeded the vendor's loss.¹⁰⁸ California courts, for example, expressly authorize defaulting purchasers, even those who willfully default, to bring separate restitution actions to recover this excess amount.¹⁰⁹

For many purchasers, however, protection against forfeiture of the modest or nonexistent equity that they have accumulated in their homes is not a primary concern. When a purchaser pays a small down payment and agrees to buy a home over a lengthy term, he is in the same position as a tenant except that he must pay taxes and insurance and, under current law, must make all needed repairs. Like a tenant, the purchaser does not hold title to the property, has no real money invested in it, and can be evicted for missing one or two monthly payments. Furthermore, the purchaser is likely to pay monthly amounts that closely approximate rent. Accordingly, this type of installment purchaser and the typical tenant are entitled to essentially the same treatment.

A purchaser can gradually build up a meaningful equity in the home if the home was not overpriced originally, if it is not in an area of declin-

¹⁰² Note, *supra* note 4, at 105-06.

¹⁰³ *Id.* at 105.

¹⁰⁴ *Id.* at 103-05.

¹⁰⁵ *Id.* at 106-08.

¹⁰⁶ See *id.* at 106-07.

¹⁰⁷ *Id.* at 102-03.

¹⁰⁸ See, e.g., *Jenkins v. Wise*, 58 Haw. 592, 598, 574 P.2d 1337, 1341-42 (1978); *Huckins v. Ritter*, 99 N.M. 560, 561-62, 661 P.2d 52, 53-54 (1983); *Heikkila v. Carver*, 378 N.W.2d 214, 219 (S.D. 1985); *Morris v. Sykes*, 624 P.2d 681, 684 (Utah 1981).

¹⁰⁹ See *Peterson v. Hartell*, 40 Cal. 3d 102, 113, 707 P.2d 232, 239-40, 219 Cal. Rptr. 170, 177-78 (1985); *Honey v. Henry's Franchise Leasing Corp. of Am.*, 64 Cal. 2d 801, 803, 415 P.2d 833, 834, 52 Cal. Rptr. 18, 19 (1966).

ing home values, and, most importantly, if the purchaser can avoid default. As a result of these and other factors, however, a purchaser often stands a very poor chance of building any true equity in a home. To illustrate, consider a home that is overpriced by ten percent at the time of the sale and that costs ten percent of its value to resell in a normal manner. The purchaser of this home must develop an equity cushion of twenty percent before he will net any money from reselling it. If the purchaser has paid only a token amount as a down payment and has agreed to buy the home in equal monthly installments over twenty years, at an interest rate of ten percent, he will begin to accumulate real equity only after more than *eight* years of payments.¹¹⁰ In other words, absent inflation in home values, a resale during the first eight years will net less than the amount needed to pay off the vendor. Thus, during the first eight years, the purchaser's plight is substantially similar to that of a tenant, who also has no opportunity to build up equity in his home.

In a state that allows forfeiture or provides a speedy foreclosure method, the vendor can quickly regain the property upon a purchaser's default. Even if foreclosure is required, the vendor, during at least the first eight years of the hypothetical loan, can recover the property and keep it, usually with an obligation to refund only payments in excess of the fair rental value of the premises.¹¹¹ Depending upon the circumstances, a vendor might reasonably expect to recover the property within this eight-year period, and the required repossession method might be only slightly more expensive and time consuming than the remedy available to a repossessing landlord. A vendor intent upon recovering property can easily increase the chance of default and property recovery by inserting into the contract a balloon payment obligation requiring the purchaser to pay the balance of the contract price in full after several years of level monthly payments. Informed buyers might object to such a clause, and financially strong buyers might succeed in getting outside financing to cover the balloon payment. But many installment buyers

¹¹⁰ As reflected in basic loan progress charts, a purchaser on the terms described in the text will have 80.7% of the principal unpaid after eight years. At an interest rate of 14%, a purchaser after 10 years has paid only 19.9% of the principal and, therefore, only at that point begins to accumulate equity (assuming no general inflation in property values).

¹¹¹ Vendors can always retain the purchaser's payments to the extent that they do not exceed the fair rental value of the property. See, e.g., 7 Powell, *supra* note 4, ¶ 938.23[4], at 84D-83 to -84. If the purchaser's monthly payments are not significantly greater than the fair rental value of the property, then the vendor can retain all amounts paid, regardless of how long the purchaser has occupied the property. See *id.* at 84D-85 (citing cases supporting proposition that restitution in most states is available only if vendor's recovery is so great as to shock conscience or amount to unfair recovery). In many states, of course, the vendor can always retain the payments, without regard to other factors, since he is under no restitution obligation. See, e.g., *Johnson v. Werner*, 63 A.D.2d 422, 407 N.Y.S.2d 28 (1978); 1 G. Palmer, *The Law of Restitution* 596 (1978).

will reach the balloon payment date with little or no cash to invest in the home and no realistic chance to avoid default. On a regular, predictable schedule, a vendor might retrieve his properties and make them available for resale.

Thus, it is easy to imagine circumstances in which an installment purchaser has no equity in a home and no reasonable prospect of building much equity, a situation in which he is the functional equivalent of a tenant. When this is true, the law should treat him as a tenant and offer him the contract and tort law protections of the implied warranty of habitability.

III

THE FUNCTIONAL EQUIVALENCE TEST

The extension of the implied warranty of habitability to the installment contract purchaser when he is the functional equivalent of a tenant is consistent with the rationales for the implied warranty and with current warranty case law.¹¹² The installment buyer, as much as a residential tenant, seeks safe, livable housing in a home free of material hazards and defects. The purchaser, like the tenant, is interested mostly in a house suitable for occupancy rather than in bare land and expects, at a minimum, toilets to flush and furnaces to heat. Because the law currently offers no protection for this expectation, the law needs to change. Furthermore, the installment vendor, like the landlord, derives monthly income from the use of property to which he holds title, and the purchaser, like the tenant, is subject to overreaching and unfair contract terms. Finally, public concerns over the quality of our nation's housing stock apply with full force in both settings.

In applying the functional equivalence doctrine, a court will necessarily place greater weight on purchaser expectations and public policy concerns than on the exact terms of the contract. Given the continuing

¹¹² Because the principle of functional equivalence is applied in mortgage law as well, the mortgage law functional equivalence doctrine may provide a useful precedent for courts. It has long been established that mortgage rules apply to any arrangement between two parties that is the functional equivalent of a mortgagor-mortgagee relationship. See, e.g., G. Nelson & D. Whitman, *supra* note 4, §§ 3.1 to .38. The form of the arrangement is immaterial except insofar as a putative mortgagor is required to prove, generally by clear and convincing evidence, that a nonmortgage arrangement in form is a mortgage in substance. See Cunningham & Tischler, *Disguised Real Estate Security Transactions as Mortgages in Substance*, 26 Rutgers L. Rev. 1, 4-8 (1972). Often a court will view a sale transaction as a mortgage in substance. G. Nelson & D. Whitman, *supra* note 4, §§ 3.7 to 3.9, 3.18 to 3.19. For example, if a property owner "sells" property to a second party and leases the property back with an option to purchase, the transaction will be viewed as a mortgage if the lease and buyback terms are similar to loan repayment terms and if the parties, after the initial sale, act more like borrower and lender than tenant and landlord. See *id.* § 3.19. Once a court views the transaction as a mortgage, all rights and obligations of the mortgage relationship apply. *Id.* § 3.9.

strength of the ideal of freedom of contract, which dominated legal thought in the late nineteenth and early twentieth centuries, many courts may be reluctant to emphasize purchaser expectations and public policy at the expense of interpreting the contract as written. However, the promise model of contract law, in which courts enforce contract terms exactly as written, has come under considerable, and deserved, criticism. In contracts affecting everyday life that are entered into without a firm, actual meeting of the minds, particularly contracts in which one or both parties lack full comprehension of meaningful contracting options, it is appropriate for courts to weigh the social context of the contract as heavily as the exact contract language. Courts need to consider the expectations of parties and the social context of contractual dealings to a greater degree than they have done so far; they need to consider general societal norms of fairness and reciprocity as well as precise party promises.¹¹³

The context of the residential installment contract demands the application of a functional equivalence doctrine. Low-income purchasers often have not meaningfully consented to the terms of their purchase contracts.¹¹⁴ They are frequently poorly advised and have little under-

¹¹³ For a fine argument for the need to consider expectations, social contexts, and societal norms in contract enforcement actions, see Lightsey, *A Critique of the Promise Model of Contract*, 26 *Wm. & Mary L. Rev.* 45, 48-62 (1984). For a more pointed criticism of "freedom" of contract, see Kennedy, *Distributive and Paternalist Motives in Contract and Tort Law, with Special Reference to Compulsory Terms and Unequal Bargaining Power*, 41 *Md. L. Rev.* 563 (1982) (arguing that judiciary considers efficiency, distributive, and paternalistic objectives as guides to decision making because free contract principles are ambiguous, unrealistic, and often conflicting).

Other commentators have discussed the social context and societal expectations surrounding property. See, e.g., Radin, *Property and Personhood*, 34 *Stan. L. Rev.* 957, 957-96 (1982) (arguing that certain property rights, such as rights to a home and warranty of habitability, are necessary to protect an individual's sense of autonomy, connection to community, and personhood). For a good recent study focusing on the importance to tenants of secure, stable housing, see Note, *Community, Home, and the Residential Tenant*, 134 *U. Pa. L. Rev.* 627, 627-56 (1986) (arguing that legal system should allow and encourage tenants to become attached to their dwellings and become "true members" of their communities).

¹¹⁴ See Barnett, *A Consent Theory of Contract*, 86 *Colum. L. Rev.* 269 (1986). Barnett provides an excellent summary of the principal theories supporting the enforcement of contracts and notes the difficulties of each. See *id.* at 271-91. The consent theory that he proposes posits that individuals have certain entitlements and that a contract results when a person consents to transfer or relinquish an entitlement to another person. See *id.* at 300-04. The consent required for a valid contract is a manifested intention to alienate rights under circumstances that imply a willingness to be legally bound. *Id.* at 304. Moreover, certain individual entitlements or rights are inalienable. Thus, transactions relinquishing inalienable rights might be unenforceable. *Id.* at 321. The functional equivalence test fits comfortably with this consent theory of contract obligation. The established warranty of habitability doctrine in landlord-tenant law suggests that absent consent (in the form of a valid waiver that meets certain tightly set requirements), the entitlement of tenants to safe, livable housing is an inalienable right. In the installment land contract setting, the purchaser should be legally unable to alienate his entitlement to safe livable housing unless similar tightly set requirements are met.

standing of the business transactions into which they enter.¹¹⁵ Moreover, while low-income purchasers often prefer to rent rather than purchase,¹¹⁶ the scarcity of rental housing¹¹⁷ may frustrate this desire.

Once a court looks beyond the contract to examine expectations and social norms, the functional equivalence doctrine gains strength. The vendor retains title to the property and reasonably expects to recover it upon default; the purchaser is required to make rentlike monthly payments and continues in possession as long as he makes them. To the outside world—and to the noncomprehending purchaser—the relationship has all the characteristics of a lease. In lease settings, expectations and public policies take precedence over contract terms. In functionally identical installment contract situations, the same approach should apply.

To phrase the functional equivalence doctrine in a different way, the habitability duty should be dependent upon whether a contracting property owner retains a certain level of control over his property and not upon whether the contracting parties execute a particular contract form. If the property owner retains title to the property, has a right to recover the property (and retain all money paid) after a missed monthly payment or two, and has a reasonable expectation of recovering the property, then a habitability duty should arise.

To be sure, courts will face difficulties in formulating a functional equivalence test. But even before reaching these difficulties, two objections might be raised to the whole idea of extending habitability protections to installment purchasers. First, installment contracts often cover single-family homes and are often sold by nonmerchant, or at least small-time, vendors. Some would argue that extending the implied warranty of habitability to those vendors would be overly burdensome and would upset their expectations, particularly for vendors who move away after selling. This objection has some merit but no more in this context than in the landlord-tenant setting. Therefore, a state that extends habitability protections to single-family tenants (as virtually all do) should not object on this ground to an extension of a protection to single-family purchasers. Moreover, a special waiver rule would solve any lingering problems. In a manner similar to the approaches of the Uniform Residential Land-

¹¹⁵ See *Mixon*, supra note 4, at 535-48.

¹¹⁶ A person may prefer renting to avoid liability for taxes and insurance, to avoid dealing with public officials over land use violations, to avoid responsibility for repairs, and to avoid the troubles that arise when he wants (or is economically compelled) to leave the property. See, e.g., *Kaplan, Bond for Deed*, supra note 12, at 1 (discussing growing practice of homes sold on bond-for-deed contracts to low-income purchasers and purchasers' unexpected obligations to pay for repairs, taxes, and insurance).

¹¹⁷ See *id.* at 3; *Whitman, Federal Housing Assistance for the Poor: Old Problems New Directions*, 9 *Urb. Law.* 1, 1 (1977).

lord and Tenant Act¹¹⁸ and the *Restatement (Second) of Property*,¹¹⁹ courts could authorize waivers of ordinary repair duties when the parties expressly and knowingly agree, when the repairs are within the technical and financial capabilities of the purchaser, and when the waiver is otherwise substantively fair.

A second objection is that an installment vendor, unlike a landlord, may lack a long-term financial interest in the property that would justify his paying for repairs of a capital nature. Although this objection calls into question the wisdom of any judicial effort to rewrite an installment contract, it has little merit when examined in the factual setting of many of these contracts, where a vendor has virtually the same expectation of recovering the property as does a landlord. In addition, the functional equivalence test can be tailored so that it affords purchasers protections only when they function as tenants. Thus, if the test is properly drawn, the habitability protections will extend only to settings in which the vendor has a reasonable expectation of property recovery. In any event, many purchaser complaints will stem from defects existing at the beginning of the contract term. It is hardly unfair to require the vendor to remedy pre-existing defects before sale; if the expense is material, the contract price can be increased accordingly. Indeed, in many cases, as in *Pines v. Perssion*,¹²⁰ a court need only find in a sales contract an implied warranty that the premises are habitable at the commencement of the purchaser's occupancy under the contract.¹²¹

A properly formed functional equivalence test, one that avoids the problem of unfair, burdensome repair duties placed on a vendor who lacks a substantial continuing interest in the property, will advance important policy goals. It will help fulfill natural and reasonable purchaser expectations. It will protect purchasers who lack the financial resources and incentives to make major home repairs. And, most important, it will promote the improvement of our nation's housing stock. Like the habitability warranty in the landlord-tenant context, habitability protections for installment purchasers can reduce urban blight and promote purchaser comfort and safety.

These benefits provide a sizable incentive for courts and legislatures

¹¹⁸ See Unif. Res. Landlord and Ten. Act § 2.104(c), 7B U.L.A. 460 (1985) (parties may agree in writing that tenant will perform repairs if agreement is in good faith and not for purpose of evading obligations of landlord).

¹¹⁹ See Restatement (Second) of Property, Landlord and Tenant § 5.6 (1977) (parties to lease may agree to alter landlord's obligations and tenant's remedies unless agreement is unconscionable or against public policy).

¹²⁰ 14 Wis. 2d 590, 111 N.W.2d 409 (1961).

¹²¹ See text accompanying note 41 supra. If a jurisdiction adopts this approach, it will avoid the problem of determining the duration of a vendor's repair obligation. The *Pines* approach is a positive step toward the adoption of the full proposal set forth in this Article.

to develop a fair and workable functional equivalence test. This test should focus on three factual questions:

- (1) Does the purchaser have little equity in the property?
- (2) Are the periodic payments by the purchaser substantially equivalent to the reasonable rental value of the property?
- (3) Is the vendor likely to recover the property?

If these three questions are answered affirmatively, the installment sale is equivalent in substance to a lease, and courts should impose habitability obligations on the vendor-landlord.

In examining the amount of a purchaser's equity, as required by the first prong of the functional equivalence test, courts should be alert to price inflation by the vendor and to contracting tricks (such as rebates or purchase price credits) that boost the purchaser's apparent equity. They should determine the real equity by calculating the resale value of the home minus the unpaid contract price.¹²² (The unpaid contract price may need to be reduced to present value if future installments do not carry a fair interest rate.)¹²³ If this difference is less than five percent of the value of the home—an arbitrary but perhaps reasonable figure—the purchaser's equity should be presumptively viewed as insubstantial.

Courts must also exercise caution in applying the second prong of the test because it may be difficult to compare monthly payments to fair rental value. For comparison purposes, a pro rata portion of taxes and insurance on the home paid by the purchaser should be added to actual monthly payments to the vendor. In determining fair rental value, courts should consider the rental value as the vendor would establish it; if the home sale price is inflated, courts can assume that the vendor would similarly inflate the rental price. The second prong is satisfied if the difference between the adjusted monthly payments and the fair rental value is insignificant. Alternatively, courts may use interest tables to determine what portion of each periodic payment reflects an equity contribution. Again, if the purchaser is paying an insubstantial amount above the

¹²² Courts should focus on the resale value of the home, net of selling expenses, rather than on the contract purchase price. The contract price may be inflated and will often be overstated because future payments do not carry a fair interest rate. See note 123 *infra*. Moreover, housing in poor repair is often hard to sell through normal realtor channels and often declines in value. A true equity figure, rather than some paper figure, is the better gauge of purchaser equity.

¹²³ An understated interest rate can dramatically increase the nominal purchase price of a home without increasing the monthly payment required of the purchaser. Assume, for example, that a purchaser buys a home and agrees to pay \$425 per month for 20 years with a \$1,000 down payment. If a below-market rate of 10% is stated in the contract, the purchase price of the house can be listed at \$45,000. If, on the other hand, the true market rate of 12% were properly stated in the contract, the purchase price of the home, given the same monthly payments and down payment, would be \$39,500. These estimates are readily obtainable from mortgage payment tables.

rental value of the property (perhaps less than ten percent), the second prong of the test is satisfied.

When applying the third prong of the test, courts should determine whether a reasonable person in the vendor's position would view recovery of the property as likely. To make this determination, courts should examine all evidence bearing on the likelihood that the vendor will regain the property, including the vendor's record in prior sales¹²⁴ and contract terms, such as large balloon payments, that increase the chance of default by the purchaser and recovery by the vendor. The most important factor will be the economic condition and motivations of the particular purchaser and other purchasers to whom the vendor is selling similar property.

If a court determines that a contract purchaser is the functional equivalent of a tenant under this test, it should impose on the vendor-landlord an obligation to make the premises habitable at the beginning of the lease and keep them habitable thereafter. The court should continue to view the contract as a lease until the purchaser holds substantial equity in the property. When the purchaser's equity interest reaches a substantial portion (perhaps ten percent) of the fair market value of the property, the vendor's habitability obligation may be terminated.

The functional equivalence doctrine, then, should operate much as the convertibility approach does, transforming an installment contract into a mortgage once the purchaser has developed some specified level of equity.¹²⁵ Here, the "lease" would become a true sale once a specified level of equity was reached.¹²⁶ In measuring equity for this purpose, courts again should look to the resale price minus the unpaid contract price because, from the purchaser-tenant's perspective, this is the only true measure of wealth. Only when the equity is substantial, from this perspective, is there a strong likelihood that the purchaser will complete the contract and the vendor will not recover the property.

¹²⁴ In assessing a vendor's record of recovery, a court need not respect the separate legal identity of individual corporations or other legal entities managed directly or indirectly by the vendor. The factual issue raised is whether the vendor realistically did expect or should have expected to regain the property that he leased. On this issue, the vendor's experiences in similar installment sales will be relevant, whether or not the similar sales were conducted through the same legal entity as the sale being contested. Indeed, a court might properly consider evidence from sales in which the vendor did not engage if the sales were on sufficiently similar terms to provide probative evidence of the realistic expectations of a person in the vendor's position.

¹²⁵ See text accompanying notes 93-96 *supra*.

¹²⁶ If a jurisdiction employs the convertibility doctrine and converts contracts into mortgages when a certain equity is reached, it may want to use the same conversion point for purposes of converting a lease into a true installment sales contract. If it does, the purchaser, upon reaching the conversion point, would be converted directly from a lessee to the status of mortgagor.

Both vendors and purchasers will benefit if courts draw lines for the functional equivalence doctrine with relative clarity and precision. When Indiana adopted the convertibility approach, it implied that vendors must foreclose when the purchaser attains a substantial equity in the property,¹²⁷ a standard that leaves all parties with considerable uncertainty. Legislatures and commentators have shown much less hesitance in setting precise percentage figures for conversion points (and in criticizing courts for their failure to do so).¹²⁸ Although precise line drawing runs counter to the common law judicial tradition, the need for it in this context will outweigh the judicial discomfort it generates.

When and so long as a purchaser is the functional equivalent of a tenant, a court should also impose on the vendor a landlord's tort duties and liabilities. A negligence standard should normally apply, with the vendor liable only for misperformance of repair duties;¹²⁹ strict liability, however, may be appropriate for large-scale merchant-vendors.¹³⁰

The purchaser should bear the burden of proving that an installment contract deserves treatment as a lease¹³¹ because it is the purchaser, after all, who disputes the chosen contract form. Once this initial burden is satisfied, the burden to show that the purchaser has obtained enough equity in the property to convert the contract from the functional equivalent of a lease to a sale should then shift to the vendor. This shift is appropriate because the vendor can fairly be required to rebut a pre-

¹²⁷ See *Skendzel v. Marshall*, 261 Ind. 226, 240-41, 301 N.E.2d 641, 650 (1973), cert. denied, 415 U.S. 921 (1974); Note, *supra* note 4, at 112.

¹²⁸ See, e.g., Ill. Ann. Stat. ch. 110, para. 15-1106(2) (Smith-Hurd Supp. 1987) (requiring foreclosure where amount unpaid is less than 80% of purchase price); Ohio Rev. Code Ann. § 5313.07 (Baldwin 1970) (requiring foreclosure where purchaser has made payments for five years or more or has paid at least 20% of the purchase price); Power, *supra* note 96, at 425 (proposing statute with precise conversion points); Note, *supra* note 4, at 112-14 (criticizing convertibility approaches that use imprecise conversion point).

A precise rule rather than a vague, flexible standard is needed. Rules provide actors with better guidance on where they stand and materially aid in planning efforts. Standards are more vague; they provide decision makers with greater opportunity to tailor justice to the specific facts of a case but thereby frustrate efforts by actors to determine their legal rights without litigation. See, e.g., Schlag, *Rules and Standards*, 33 UCLA L. Rev. 379 (1985).

¹²⁹ See text accompanying note 65 *supra*.

¹³⁰ There is disagreement over the appropriate standard for large-scale merchant-vendors. Compare *Becker v. IRM Corp.*, 38 Cal. 3d 454, 464-65, 698 P.2d 116, 122, 213 Cal. Rptr. 213, 219-20 (1985) (holding landlord in business of leasing dwellings strictly liable for injuries caused by latent defect in premises existing when premises were let to tenant) with *Browder*, *supra* note 59, at 118-23, 135-41 (concluding that strict liability is unlikely to find wide acceptance in landlord-tenant cases).

¹³¹ Cf. R. Cunningham, W. Stoebuck & D. Whitman, *supra* note 3, § 11.1, at 720 (party seeking reformation of deed carries burden of presenting clear and convincing proof); G. Nelson & D. Whitman, *supra* note 4, at § 3.7, at 47-48 (party claiming that sale is functional equivalent of mortgage has burden of proof and usually must produce clear and convincing evidence).

sumption that has been established against him. If the court finds that a contract should be treated as a lease, the purchaser should have the normal tenant remedies for breaches of the warranty of habitability, including the right to repair defects and deduct the costs of repair from monthly payments and the right to reduce monthly payments by the diminution in value caused by any continuing disrepair.¹³² Because disputes are likely, courts should insulate purchasers who have made reasonable, good faith efforts to assert their rights against claims of forfeiture.

The functional equivalence doctrine can be kept within limits. When applicable, it will only impose habitability duties in contract and tort. In all other respects, courts should respect the installment contract format if they would otherwise do so under state law.¹³³ They need not attempt, even temporarily, to insert lease terms, termination rights, and various other landlord and tenant covenants. Absent fraud or misrepresentation (and perhaps innocent mistake justifying rescission),¹³⁴ the purchaser can enjoy the normal protections against hasty forfeiture,¹³⁵ and the landlord can declare a forfeiture and recover the property to the extent otherwise allowed. The functional equivalence doctrine, in short, need not bog courts down in trying to write a lease when none really exists.

Although the functional equivalence doctrine may seem unduly one-sided because it imposes obligations only on the vendor and provides benefits only to the purchaser, it can operate as fairly and justly as the implied warranty in express leases, an application that is broadly accepted.¹³⁶ Once a jurisdiction develops the doctrine, vendors will have notice of their duties and can price their properties accordingly. Only vendors who are caught with contracts in midstream will be unfairly surprised by the new doctrine. Even these vendors will be burdened only until the tenant-purchaser accumulates sufficient equity in the property to justify conversion. Burdens of this type are an accepted, and indeed, familiar part of the common law judicial process when new rules are

¹³² See R. Schoshinski, *supra* note 16, at 132-44, 159-78.

¹³³ A court need not, of course, respect the contract form if it would ordinarily treat the purchaser as a mortgagor in all cases. See, e.g., *Sebastian v. Floyd*, 585 S.W.2d 381 (Ky. 1979). Other public policy concerns might also justify ignoring the contract form in some other respects.

¹³⁴ See Freyfogle, *Real Estate Sales and the New Implied Warranty of Lawful Use*, 71 *Cornell L. Rev.* 1, 5-32 (1985) (discussing home buyer's possible recovery for misrepresentation and nondisclosure, and grounds for rescission and restitution relief). If the vendor knows that the purchaser is extremely confused and the vendor remains silent, a court might properly grant reformation relief to transform the putative sales contract into a periodic tenancy lease and thus extend to the purchaser the full range of tenant rights.

¹³⁵ See text accompanying notes 87-107 *supra*.

¹³⁶ See note 16 *supra*.

introduced. In this setting, the burdens caused by surprise are not weighty enough to justify rejection of the doctrine, but a legislature adopting the doctrine might well choose a prospective application. Application only to contracts executed after the doctrine takes effect fully removes the surprise element. Moreover, many properties that vendors repair will return to them after default by a purchaser. When this happens, vendors will benefit belatedly from their own repair efforts because the property will return to them in its improved condition. If the purchaser avoids default and continues regular payments, he will eventually reach the conversion point, after which the purchaser has no right to demand repairs.

As its principal benefit, the functional equivalence doctrine should encourage vendors to avoid selling dilapidated property on contract. If it does so in even a modest way, the new doctrine can be viewed as a success. Although evidence is unavailable, it seems likely that most purchaser complaints will involve major defects existing at the beginning of the contract term. Once property is properly made habitable, it should need few major repairs during the limited term of the landlord's repair duty. The doctrine, then, should encourage vendors to repair property before they sell it. Once the repairs are made, sale will be easier and the property may even command a higher price. Vendors should soon realize that they benefit more by repairing major defects before, rather than after, the sale—a course of conduct that would reduce disputes.

The functional equivalence doctrine should encourage vendors faced with the prospect of habitability duties under installment contracts to avoid sales and lease their properties instead. While leases would impose the same habitability duties (at least in the short term), they would offer other substantial benefits to the landlord. Unlike a vendor, a landlord can raise the rent and evict tenants upon proper notice.¹³⁷ If major repairs add substantial value, a landlord can recoup some of his investment through higher rents. Repossession after default may also be easier,¹³⁸ although a landlord must return security deposits while a vendor can retain modest down payments after forfeiture.

If, as a result of the new doctrine, most property owners turned to leases instead of installment contracts, the functional equivalence doc-

¹³⁷ See, e.g., *David Properties, Inc. v. Selk*, 151 So. 2d 334 (Fla. Dist. Ct. App. 1963) (stating that landlord can raise rent unilaterally at commencement of new lease term); R. Cunningham, W. Stoebuck & D. Whitman, *supra* note 3, §§ 6.71 to .74 (1984) (discussing means by which parties can terminate lease). In the case of public housing and rent-controlled apartments, however, landlords generally face limits on their power to evict. See *id.* § 6.79.

¹³⁸ In most states, landlords can recover possession after a tenant's default by using a summary repossession method, often called a forcible entry and detainer action. See R. Cunningham, W. Stoebuck & D. Whitman, *supra* note 3, § 6.77.

trine would give rise to little new litigation. Disputes over leased premises would be resolved under the established habitability doctrine of landlord-tenant law. The primary effect of the new doctrine, therefore, might simply be to bring subterfuges to a halt—to prevent the use of the installment contract format except in cases in which the landlord truly expects to part with the property.

In some cases, to be sure, a vendor might choose to refuse an installment sale because the new functional equivalence doctrine imposes weighty burdens. The vendor might take the property off the market and thereby deplete the stock of modestly priced housing. Alternatively, the vendor might raise the price of the house to the point where low-income buyers could not afford it. These actions, of course, would all be undesirable, and it is difficult to offer proof that they would not occur. Yet, these same arguments were presented in opposition to the habitability warranty in residential leases, a setting in which they might seem to have even greater force. They were rejected in that setting, with few harsh results.

In adopting the warranty for leases, states decided as a fundamental policy matter that landlords should have no right to offer, and tenants no right to acquire, substandard housing. They decided to upgrade the housing stock by insisting that all leased residences meet minimum standards, even if the effect was to push up rents or force dilapidated property off the market. The same policy position is equally applicable in this setting, and it should govern. The habitability warranty did not noticeably reduce the housing stock, and its extension to certain installment sales is not likely to do so either. In some cases purchasers will face higher prices, but they will be getting better (if still only minimal) homes. More likely, vendors are already charging what the market will bear, and they will have little ability to raise prices. In any case, an installment vendor dissatisfied with the new warranty still retains the options of leasing or selling on a contract that is not the equivalent of a lease. With these other options, the vendor's plight is hardly so onerous as to give cause to reject an otherwise appropriate extension of the habitability doctrine.

CONCLUSION

The implied warranty of habitability has been one of the most popular and successful reform efforts of the past two decades. It gave tenants a powerful tool to demand livable housing. Like all legal tools, it does little for the beneficiary who is unaware of his rights or unwilling to assert them. Moreover, it is a tool that may yet lack the strength to deal with determined slumlords who act in concert to keep down the quality

of rental housing in a particular area.¹³⁹ Nevertheless, it is a valuable doctrine that has aided in improving the quality of rental housing in state after state. A property owner should not be able to circumvent the implied warranty of habitability's protections by selecting a contract form other than a lease. Courts and legislatures have prohibited waivers of the implied warranty in nearly all cases in order to protect tenants and to preserve the public benefits of clean, safe housing. The functional equivalence doctrine proposed in this Article simply extends that no-waiver rule and grants habitability protections in contract and tort to the installment purchaser who is functionally indistinguishable from a tenant. Moreover, it would preserve those protections until the purchaser builds up enough equity to be regarded as more than a typical tenant. Properly constructed, the doctrine will aid low-income families, either by protecting them as purchasers or restoring them to the better-protected tenant status. The functional equivalence doctrine will extend to the installment home buyer the many private and public benefits that account for the habitability warranty's considerable popularity today.

¹³⁹ See S. Brakel & D. McIntyre, *The Uniform Residential Landlord and Tenant Act (URLTA) in Operation: Two Reports*, 1980 *Am. B. Found. Research J.* 555 (reporting that studies on impact of URLTA in Oregon and Ohio indicate little improvement in quality of inner-city housing); Salsich & Fitzgerald, *Mediation of Landlord—Tenant Disputes: New Hope for the Implied Warranty of Habitability?*, 19 *Creighton L. Rev.* 791, 792-93 (1986) (stating that warranty of habitability has not improved housing conditions of low- and moderate-income tenants).