

## QUESTION 2

Steve agreed to convey his condominium to Betty for \$200,000 in a written contract signed by both parties. During negotiations, Steve told Betty that, although there was no deeded parking along with the unit, he was allowed to park his car on an adjacent lot for \$50 a month. Steve stated that he had no reason to believe that Betty would not be able to continue that arrangement. Parking was important to Betty because the condominium was located in a congested urban area.

On June 1, the conveyance took place: Betty paid Steve \$200,000, Steve deeded the condominium to Betty, and Betty moved. She immediately had the entire unit painted, replaced some windows, and added a deck. The improvements cost \$20,000 in all. She also spent \$2,000 to remove the only bathtub in the condominium and to replace it with a shower, leaving the condominium with two showers and no bathtub.

On August 1, Betty discovered that the owner of the adjacent parking lot was about to construct an office building on it and was going to discontinue renting parking spaces. She also learned that Steve had known about these plans before the sale. She quickly investigated other options and discovered that she could rent parking a block away for \$100 a month. At the same time, she also found that, immediately before Steve had bought the condominium, the previous owner had been murdered on the premises. Steve had failed to tell Betty about the incident.

Betty has tried to sell the condominium but has been unable to obtain offers of more than \$160,000, partly due to the disclosure of the murder and the lack of a parking space. Betty has sued Steve for fraud.

What is the likely outcome of Betty's lawsuit and what remedies can she reasonably seek? Discuss.

## QUESTION 2: SELECTED ANSWER A

### Steve's Breach in Respect of the Parking Space

The issue is whether Steve misrepresented to Betty the facts relating to the parking space in a way that would give cause to a right of action.

A misrepresentation is a (i) statement of fact, (ii) that is false, and (iii) either material or the known to the declarant to be untrue, and (iv) which induces a person to act to their detriment in reliance on the representation.

Steve made a clear statement of fact when he said there was an existing parking space available for rent at \$50 a month and he had no reason to believe that the arrangement would not be continued. This fact is clearly false since the construction of an office building means that the parking arrangement will be discontinued.

Steve told Betty that he saw no reason she could not continue to park her car subject to the pre-existing arrangement (payment of a \$50 a month fee). Parking was important to Betty given the nature of the area (a congested urban area) - a fact that Steve should have been aware of, having lived in the area himself. Betty will argue that this was a material fact of importance in her decision to enter into the condo sale. Steve will argue the opposite, that parking is ancillary to the property purchase and therefore lacks the materiality required for misrepresentation. As Betty later discovered, Steve knew about the plans to discontinue renting parking spaces before the sale occurred, therefore even if the statement is not considered material it will satisfy the requirement of knowledge that it was untrue.

Given the importance of parking to Betty, she will argue that the fact there was a parking arrangement in place was central to her decision to purchase the condo and she therefore acted in reliance on the statement. Again, Steve will try to argue that the parking is ancillary to the condo, it was not part of the deeded property and does not

sufficiently constitute reliance as there must have been many other factors that induced Betty to purchase the condo such as price, size and location.

Given that parking is something Betty probably does on a daily basis, the existence of adequate parking arrangements is likely to be viewed by the courts as sufficient motivation for reliance. Therefore Steve's statement is indeed likely to be viewed as a fraudulent misrepresentation.

### Failure to Disclose the Murder

The issue is whether Steve was under a duty to disclose that a murder had previously occurred in the condo.

At common law, the seller of property had no duties of disclosure to the buyer, under the doctrine of caveat emptor. The buyer was entitled to inspect the property prior to purchase and had the obligation to discover any defects for herself. The modern trend is to impose on sellers a duty to disclose material defects of which the buyer was not aware and could not easily discover on inspection. Liability for failure to do so arises under the principles of concealment and fraud.

The fact that a murder had taken place in the condo itself is a fact very likely to affect the marketability of the condo. Indeed Betty found the value had dropped significantly once she disclosed this fact to potential new buyers. Betty will argue that Steve had a duty to actively disclose this information to her and his failure to do so constituted fraud. Steve, on the other hand, will argue that he made no representation about the murder and never stated that a murder had not happened and therefore cannot be found liable for fraud because he did not do or say anything dishonest.

The courts will likely find that Steve did have a duty to disclose this information to Betty, as it is a material fact concerning the property that will have an adverse effect on its value. Steve's failure to disclose will amount to concealment and consequently Betty should have a strong course of action against Steve for fraud.

## Appropriate Remedies

Where there is fraud in the inducement of a contract, the contract becomes voidable and entitles the innocent party to treat the contract as void and seek remedies accordingly.

The appropriate remedies for Betty will depend on whether she wishes to stay in the condo, but make good her financial loss, or whether she wishes to force a sale of the property and move out.

## Money Damages

If Betty decides to stay in the condo the most appropriate course of action will be to affirm the contract and seek money damages. The various money damages rules are all aimed at compensating for loss of expectation, where the expectation was simply no breach. Expectation damages will be used to put the plaintiff in the position she would have been in had the contract been as expected. In order to claim damages, the claimant must show that (i) the defendant's actions were the cause of the loss, (ii) the loss was reasonably foreseeable at the time the contract was entered into, (iii) the loss is certain and not too speculative, and (iv) it was unavoidable (meaning the claimant has taken all steps available to reduce her loss).

For the Parking Space - With respect to the parking, Betty's expectation was that she would have a place to park her car for \$50 a month. Steve's misrepresentation is the clear cause of this loss and it was reasonably foreseeable at the time that if Steve's statement about the parking was false, Betty would suffer damage by either having no parking or potentially having to pay more for it. Betty has taken appropriate steps to find an alternative parking space and thereby mitigate her loss. But the parking space will be twice the cost of what she was expecting. This loss is certain in monetary terms (a clear \$50 per month). Therefore Betty should have a successful claim against Steve for monetary damages to make good the loss of the parking place.

Judgment for money damages is normally made in one lump sum payment, discounted to today's value without taking account of inflation. However, the modern trend of some courts is to allow for inflation.

For the Loss in Value Due to the Murder - The courts will apply the same test to ascertain damages in respect of the drop in the condo's value due to the murder.

As before, the causal link is clear - Steve's failure to disclose the murder resulted in Betty paying an inflated price for the condo; this was foreseeable at the time, since it is clear to reasonable people that such a fact would necessarily result in the property being less marketable. Betty has attempted to sell the house but has been unable to do so for more than \$160,000; therefore the measure of expectation damages will be \$40,000. However, Betty has also spent \$22,000 on making improvements to the condo and she will argue that they have raised the value of the condo and she should therefore be able to recover for these too under the consequential damages rule. Consequential damages may be sought in order to compensate the claimant for losses over and above expectation damages that were foreseeable.

Steve will argue that removing the only bathtub in the condo has in fact depreciated the property and that the drop in value is more due to this than the disclosure of the murder.

### Rescission

Rescission is an equitable remedy that the courts may use in their discretion when there is no available legal remedy. Rescission would allow Betty to treat the contract as void, the condo would be returned to Steve and her purchase money would be returned to her.

If Betty decides she no longer wants to live in the condo, this would be a more appropriate remedy. Since land is always considered unique, Betty may argue that the legal remedy of damages is not appropriate and she should be entitled to avoid the contract altogether.

In addition to obtaining back her purchase money, Betty could seek reliance damages for the amounts spent on improving the property. Reliance damages seek to put the claimant in the position she would have been in had she never entered into the contract.

This would allow Betty to recover the \$22,000 spent on improvements.

## QUESTION 2: SELECTED ANSWER B

### **Valid Contract:**

Governing Law:

The UCC governs contracts for the sales of goods. The common law governs contracts for services, the sale of land, and all others not under the UCC.

Here, the contract was for the sale of a condominium (condo) which is real property; thus the Common Law applies.

Contract formalities:

A valid contract requires: 1) offer, 2) acceptance, and 3) consideration. Further, a land sale contract must be in writing to satisfy the statute of frauds (SOF).

Here, there is a written contract by both parties relating to the sale of the condo, thus this satisfies the SOF. Steve agreed to sell Betty his condo for \$200,000. Thus, this was a valid offer. On June 1, the conveyance took place. Steve deeded the condo to Betty; she paid the \$200,000 and moved in. Thus, Betty accepted.

Thus, the parties had a valid contract.

### **Breach of Contract:**

A breach of contract occurs when one of the parties fails to perform on the contract. With land sale contracts, once the conveyance is made, it extinguishes the contract and the parties can only sue on the deed and based on which future covenants were granted in the deed (further assurances, quiet enjoyment, or warranty).

Here, the conveyance had already occurred; thus the deed will control and Betty will not be able to sue for breach of contract relating to the land sale. However, a party can

nonetheless sue based on fraud if there was an intentional failure to disclose. If Betty can establish that there was fraud, she would be entitled to sue on a fraud theory.

**Fraud:**

Fraud requires 1) a misrepresentation, 2) of material fact, 3) known to induce reliance, 4) actual reliance, and 5) damages.

Parking:

On August 1, Betty discovered that the owner of the adjacent parking lot was about to construct an office building on it and would discontinue renting parking spaces and Steve knew about these plans. Here, there was a misrepresentation because during negotiations Steve told Betty that although there was no deeded parking, she would be allowed to park on an adjacent lot for \$50 per month just as he had. Meanwhile he knew about the building owner's plans that Betty would not be able to park in that lot. Thus, there was a misrepresentation.

This was a material fact because parking was important to Betty because the condo was located in a congested urban area. The materiality is further evidenced by the fact that she is having a hard time reselling the condo because of the parking.

Further, Steve knew this misrepresentation would induce reliance because he told Betty that he had no reason to believe that Betty would not be able to continue that arrangement. This shows that he knew that Betty would rely on this fact in deciding to continue with the purchase.

The next element is met because Betty actually relied on the misrepresentation because she decided to continue with the purchase of the condo and she did not know about the lack of parking until after the sale had been completed.

Betty's damages are established because she will lose lost the ability to park in the

nearby lot.

Thus, there was a misrepresentation as to the parking.

**Murder:**

A misrepresentation does not have to be a lie, but can be an omission as well, if the seller knew of the defect and failed to inform the buyer of the defect.

Here, Betty learned in August, some two months after the purchase, that the previous owner had been murdered on the premises, and Steve failed to disclose to Betty about the incident. Steve knew about the murder but failed to disclose it to Betty. Such a failure to disclose would amount to a misrepresentation based on omission. Here, he knew that this was a material fact because a prospective buyer would want to know if a person had been murdered on the premises. Further, the failure to disclose such a horrible fact would result in an innocent buyer to rely on the fact that no such murders had occurred on the premises. He knew that if he disclosed the murder, Betty would back out of the deal. Further, Betty relied on the fact that there had been no murders in the condo when she decided to proceed with the sale. Had she been informed about the murder, she could have had the opportunity to decide if she nonetheless wanted to continue with the purchase. Lastly, Betty has suffered damages because she cannot sell the house for more than \$160,000, partly because she has to disclose the murder to prospective buyers.

Thus, there was a misrepresentation about the murder.

In conclusion, because Steve engaged in fraud for the misrepresentation of the parking situation and the murder, Betty will be successful in her suit against Steve.

**Rescission:**

A contract can be rescinded based on a mutual mistake or fraud.

Here, Betty will seek that the contract be rescinded because she can successfully assert her claim for fraud against Steve, as established above.

**Reliance:**

Reliance damages can be obtained to avoid any unjust enrichment on the part of the defendant. Reliance seeks to put the non-breaching party in the position as if there had been no contract.

Here, Betty was excited to own her own condo. In anticipation of living in the condo for a long period of time, she decided to make improvements to it. Betty immediately had the entire unit repainted, replaced windows and added a deck. The total value of improvements cost \$20,000. She also spent \$2,000 to remove the only bathtub and replace it with a shower. Betty made such improvements because she had relied on the fact that there were no defects with the property. It would be unfair to rescind the contract and return the condo to Steve with \$22,000 worth of improvements. Thus, Betty should be able to receive reimbursement for the \$22,000 she expended on improvements to the condo.

**Expectation:**

Expectation damages seek to put the non-breaching party in the same position as if no breach had occurred.

Betty will seek expectation damages to put her in the same position as if she had never purchased the condo. When she purchased the condo she expected to live in a unit with nearby parking and no previous murder. But due to Steve's fraudulent misrepresentations, Betty will not be able to do so. As a result, Betty should be compensated as if no contract had occurred.

Betty has tried to sell the condo, but is unable to get offers of more than \$160,000 because of the disclosure of the murder and the lack of parking. If Betty sells the condo for \$160,000, Steve will be required to pay her for the difference in the original sale

price (\$200,000) and the sale price of the condo. Assuming she can get \$160,000 for it, Steve will be required to pay Betty \$40,000.

Thus, Betty is entitled to \$40,000 in expectation damages.

**Incidental:**

Incidental damages are those damages that the non-breaching party incurs as a result of the breach.

Here, Betty will be entitled to any funds expended in the attempt to sell the condo, such as brokerage fees and listing fees. Further, she should be able to recover the difference of the \$50 to park in the current parking lot and the \$100 to park in the other lot, until the condo sells.

**Punitive Damages:**

Punitive damages seek to punish the defendant for willful and wanton misconduct. Generally, punitive damages are not awarded for breach of contract actions. However, a plaintiff may recover punitive damages if there is an underlying tort.

Here, Betty's underlying theory for suit against Steve is for fraud, and fraud is a tort. The court may be compelled to grant Betty punitive damages to punish Steve for his fraudulent actions, and to teach him a lesson.

Thus, Betty may be able to recover for punitive damages.

**Limitations on Damages:**

Damages must be causal, certain, foreseeable and mitigated.

Here, Betty's damages are caused by Steve's fraud. Her damages are certain because we can place an exact dollar figure on her damages. Her damages are foreseeable

because it was foreseeable that she would have to obtain parking at another parking lot which could cost more money. It was also foreseeable that when she discovered the murder in the condo, she would not want to live there, thus motivating her to move out and sell the property. Lastly, damages must be mitigated. This means that Betty must make a good-faith attempt to sell the condo for a reasonable sum of money and within a reasonable time. Further, until she sells the property she will be

### **Steve's Defenses:**

#### **Parol Evidence Rule:**

The Parol evidence rule (PER) seeks to prohibit prior oral negotiations of a contract because the parties intended to put their final expression in the writing itself.

During negotiations Steve told Betty that there was no deeded parking but she would be allowed to park on an adjacent lot for \$50 per month, just as he had. Steve will argue that because such communications were oral and prior to the final contract, that the court should exclude them. This defense will fail because his actions constituted fraud, and the contract had already been performed.

#### **Laches:**

Laches seeks to bar a plaintiff's recovery if they wait too long to assert a claim and such delay of time causes an undue prejudice to the defendant.

Here, the sale occurred in June and Betty is suing in August. Thus, this was only a three month period and not an unreasonable delay.

#### **Unclean Hands:**

The court of equity will not aid suitors who come to the court with unclean hands.

Here, Betty did not engage in any misconduct. Rather, she was an innocent purchaser. Thus, this defense too will fail.