Commodo Caveo: Lender Beware - An Analysis of Lender Liability for Construction Defects under the Implied Warranty of Habitability

Margaret N. Fox

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COMMODO CAVEO: 
“LENDER BEWARE”—AN ANALYSIS OF LENDER LIABILITY FOR CONSTRUCTION DEFECTS UNDER THE IMPLIED WARRANTY OF HABITABILITY

I. INTRODUCTION

The recent holding of the South Carolina Supreme Court in Kirkman v. Parex, Inc.1 outlines a two-part test for courts to use in evaluating potential lender liability under the implied warranty of habitability.2 In its disagreement with the lower courts’ determinations that First Union was not subject to implied warranty liability because it was a “mere lender,” the court held that there remained an issue of material fact as to whether the lender was “substantially involved” in the completion of the Kirkmans’ home.3 An affirmative finding of substantial involvement denotes that the lender impliedly warranted the home.4 Following a finding of substantial involvement, the second inquiry outlined by the court is whether the lender effectively disclaimed the implied warranty of habitability.5

The court’s decision in Kirkman deviates from the techniques adopted by courts in other jurisdictions that have considered the issue of lender liability.6 The decision, however, is sound as a matter of policy because it protects the important social interest of caveat venditor, thus affording the buyer of a new home protection against latent defects. Such protection is a significant issue in South Carolina as there has been an increase in the number of building permits granted for new privately-owned housing units within the state,7 demonstrating the continued intention of builders and residents to construct new homes in the state.8 With the

2. Id. at 868, 632 S.E.2d at 858.
3. Id. at 863–85, 632 S.E.2d at 857–58.
4. See id. at 868, 632 S.E.2d at 858 (holding that lenders meeting the first prong of substantial involvement but failing to effectively disclaim the implied warranty are subject to judicial determination of whether the warranty was breached).
5. See id. at 868, 632 S.E.2d at 858.
6. See generally Jeffrey T. Walter, Annotation, Financing Agency’s Liability to Purchaser of New Home or Structure for Consequences of Construction Defects, 20 A.L.R.5th 499, 507–09 (1994) (stating that lender liability “has not [been] met with widespread judicial acceptance” and presenting scenarios in which courts have denied and upheld lender liability to purchasers not in privity with the lender).
8. The residential housing market in South Carolina began to decline in 2006. MOORE SCH. OF BUS., UNIV. OF S.C., SOUTH CAROLINA RESIDENTIAL CONSTRUCTION, http://moorecms.graysail.com/moore/research/Publications/Indicators/data/resc.html (last visited Mar. 6, 2008). Nonetheless, lender liability for breach of warranty is likely to remain significant. Indeed, if some builders face financial difficulty or even bankruptcy, banks may face even more claims.
average purchase price of a home being $160,000,\(^9\) purchasers likely will turn to lenders for financing options; therefore, the recent increase in the construction of new homes has created the potential for lender liability and has magnified the significant impact Kirkman could have on lenders.

Lenders likely will face problems arising from this decision, as it leaves them uncertain in determining what constitutes substantial involvement\(^10\) and how they will meet the stringent burden of proof in showing that the contracting parties “specifically bargained for” a disclaimer of the implied warranty of habitability.\(^11\) Should this uncertainty create substantial problems for lenders, this Note proposes an alternative whereby South Carolina could enact legislation requiring a lender to offer insurance covering latent defects if the lender disclaims the implied warranty of habitability.

Part II of this Note discusses the development of the implied warranty of habitability during the South Carolina Supreme Court’s movement from applying *caveat emptor* to applying *caveat venditor* in the sale of new homes. Additionally, this Note compares South Carolina lender liability cases with those in other jurisdictions that impose tort and contract liability upon lenders who are in essence “joint venturers.” Part III outlines the facts of the Kirkman decision and discusses the two requirements a court will use in determining lender liability—substantial involvement and a three-part test for an effective disclaimer.\(^12\) Part IV discusses the uncertainty lenders will face in attempting to discern conduct constituting substantial involvement. This uncertainty results from the lack of caselaw illustrating situations when this standard is met. Part V illustrates that this uncertainty of substantial involvement joins with a lack of direction given to lenders in determining how to prove a lender and seller specifically bargained for a disclaimer. While it appears a lender could fulfill the “conspicuous” and “known to buyer” requirements through a standard form with a signature requirement, there is little indication of what factors illustrate a specifically-bargained-for disclaimer other than a reduction in the price of the new home.\(^13\) Part VI proposes the enactment of a statute that would ensure protection of buyers from latent defects by requiring lenders to offer insurance if they disclaim the implied warranty of habitability. The acquisition of such insurance by lenders or their developers aligns with the sound policy implications of Kirkman by ensuring the buyer receives the benefit of the bargain from a party better situated to protect against latent defects. Additionally, such an alternative would provide a better option for lenders and

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12. See id. at 485, 632 S.E.2d at 858.

13. See id.
buyers because it would ensure the availability of adequate protection in covering defects while decreasing the potential for litigation expenses.

II. BACKGROUND OF THE IMPLIED WARRANTY OF HABITABILITY

A. Development of the Doctrine

Until 1960, the doctrine of caveat emptor—“let the buyer beware”—controlled the majority of land transactions between a home buyer and a seller of undeveloped land.¹⁴ Because sellers sold undeveloped land, the seller rarely faced implied warranty claims for construction defects; the buyer could bring claims against the architect or contractor with whom the buyer was in privity for construction defects.¹⁵ After World War II, the dramatic increase in the need for housing set the stage for a rapid rise in the construction of homes.¹⁶ Accordingly, builders began to “sell the house and the land together in a package deal.”¹⁷ As a result, purchasers were no longer able to supervise construction,¹⁸ leading to a decline in the quality of building.¹⁹ Thus, buyers of defective homes began seeking recovery from builders, challenging the doctrine of caveat emptor,²⁰ while commentators called for modification of this doctrine.²¹

Initially, caveat emptor governed real estate transactions within South Carolina;²² as a result, the seller of a new home was unaccountable for the quality of the dwelling absent an express guarantee or warranty to the purchaser.²³ South Carolina courts, along with the majority of jurisdictions, have shifted from caveat emptor to caveat venditor to provide buyers greater protection from physical defects.²⁴ The shift began with Rogers v. Scyphers,²⁵ a case in which the South Carolina Supreme Court held that when the vendor of a new home is also the


¹⁵. See Kennedy, 299 S.C. at 342, 384 S.E.2d at 735.

¹⁶. Id. at 343, 384 S.E.2d at 735; Tronquet, supra note 14, at 1253.

¹⁷. Lawrence, supra note 14, at 53 (quoting E. F. Roberts, The Case of the Unwary Home Buyer: The Housing Merchant Did It, 52 CORNELL L.Q. 835, 837 (1967)) (internal quotation marks omitted).

¹⁸. Kennedy, 299 S.C. at 343, 384 S.E.2d at 735.


²⁰. Id. at 1254.

²¹. Lawrence, supra note 14, at 53 (“[M]odern day changes in home-buying practices . . . increased pressure . . . to abandon or modify the ancient doctrine [of caveat emptor].”).


builder, the vendor may be liable for breach of implied warranty damages upon sale of the home.\(^{26}\) In Rogers, the court acknowledged its support for the trend in other jurisdictions to recognize liability based solely on the theory of implied warranty.\(^{27}\) The court premised such support on the inability of buyers to properly inspect a home for latent defects due to their lack of knowledge of the complexities involved in construction.\(^{28}\)

Subsequently, in Rutledge v. Dodenhoff,\(^{29}\) the court formally accepted the theory of "caveat venditor."\(^{30}\) Following the purchase of a new home from a builder-vendor, the buyer experienced flooding due to the builder's improper placement of the septic tank and field drains in the rear of the house.\(^{31}\) Affirming a judgment of defective installation,\(^{32}\) the court noted that buyers need the protection of an implied warranty of habitability because they must frequently rely on the seller as an expert in construction.\(^{33}\) The court based this conclusion on the fact that buyers are often "precluded from making a knowledgeable inspection of the completed house . . . because of the expense and . . . because the defects are usually hidden rendering inspection practically impossible."\(^{34}\) Finally, the court held that there existed in the sale of a new home by a builder-vendor an implied warranty that the house is suitable for habitation.\(^{35}\) Almost twenty years later, the South Carolina Supreme Court noted that Rutledge established the implied warranty of habitability "as an independent covenant which survives delivery of the deed," effectively abrogating "the doctrine of merger by deed."\(^{36}\)

In subsequent cases the court applied and extended the doctrine of the implied warranty of habitability with regard to the sale of new homes on the basis "that a sound price warrants a sound commodity."\(^{37}\) In Lane v. Trenholm Building Co., the court held that a developer-seller who did not build the home was subject to implied warranty liability\(^{38}\) for the presence of a faulty septic tank.\(^{39}\) Because the developer held itself out to the consumer as one in the business of selling homes and as one aware of the buyer's intention to provide a home for his family, the court's finding of an implied warranty effectively fulfilled the expectations of the parties.\(^{40}\)

Following the court's departure from the doctrine of merger by deed in Rutledge,\(^{41}\) Terlinde v. Neely\(^{42}\) abandoned the requirement that a buyer be in privity.

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26. Id. at 133, 161 S.E.2d at 83.
27. Id. at 134, 161 S.E.2d at 83.
28. Id. at 135, 161 S.E.2d at 84.
30. See id. at 414, 175 S.E.2d at 795.
31. Id. at 410–11, 175 S.E.2d at 793–94.
32. Id. at 411–12, 175 S.E.2d at 794.
33. Id. at 414, 175 S.E.2d at 795.
34. Id.
35. Id.
38. Id. at 503–04, 229 S.E.2d at 731.
39. Id. at 500, 229 S.E.2d at 729.
40. Id. at 503, 229 S.E.2d at 731.
41. See supra text accompanying note 36.
42. 275 S.C. 395, 271 S.E.2d 768 (1980).
of contract with the builder. In *Terlinde*, the buyer purchased a home built for speculative sale—“not pursuant to any contract with a purchaser.” As such, the buyer was not in privity of contract with the builder. Upon discovery of foundation problems within the home, the buyer brought several claims against the builder, including a claim for breach of an implied warranty. Rejecting the builder’s privity defense, the court relied on the reasoning in *Lane*, stating that an implied warranty “springs from the sale” of the new home. Moreover, if the purchaser does not know the builder of the house, the purchaser still relies on the expertise of the builder. Thus, an implied warranty against latent defects extends to subsequent purchasers of a new home.

Finally, in *Arvai v. Shaw*, the South Carolina Supreme Court held that implied warranty liability should fall on the source that places the defective home into the stream of commerce by initial sale. In noting that the “implied warranty of habitability has its roots in the execution of a contract for sale,” the court held that “[t]he determining factor is not whether the defendant actually builds the defective house, but that he places it, by the initial sale, into the stream of commerce.” Accordingly, the court’s holding set the stage for a lender who is also the seller of the home to be subjected to the implied warranty of habitability.

**B. Application of Caveat Venditor to Lenders**

In most jurisdictions, a mere lender is not liable to the purchaser of a new home for construction defects. Instead, the buyer traditionally looks to the builder or contractor for relief in tort or contract for construction defect claims. However, with the emergence of construction lenders becoming joint venturers by assuming the role of the developer or seller of the new home, the question emerges as to whether the buyer’s contract remedies should extend to the lender.

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43. *Id.* at 398–99, 271 S.E.2d at 769–70.
44. *Id.* at 396, 271 S.E.2d at 768.
45. *Id.*
46. *Id.* at 395–96, 271 S.E.2d at 768.
47. *Id.* at 398, 271 S.E.2d at 769 (quoting *Lane v. Trenholm Bldg.* Co., 267 S.C. 497, 500, 229 S.E.2d 728, 729 (1976)) (internal quotation marks omitted).
48. See *id.* at 399, 271 S.E.2d at 770 (“[I]t is clearly foreseeable that more than the original purchaser [of a home] will seek to enjoy the fruits of the builder’s efforts.”).
49. *Id.*
51. *Id.* at 164, 345 S.E.2d at 717.
52. *Id.* (citing Redarowicz v. Ohlendorf, 441 N.E.2d 324 (1982)).
53. *Id.*
54. See Walter, *supra* note 6, at 507–08 (stating that liability will only be imposed on lenders because of contractual provisions or lender assurances, or where lender activity exceeds that of a mere lender).
55. *Id.* at 507.
1. Lender Liability in Other Jurisdictions

In Connor v. Great Western Savings & Loan Ass'n, the California Supreme Court held that lenders will be liable in tort when they are an “active participant” in the construction of a new home and subsequently breach a duty of care to the buyers due to construction defects in the home. In Connor, the buyers discovered cracks in the foundation of their homes as a result of soil expansion and brought suit against Great Western for breaching an independent duty of care. Relying upon its own precedent, the California Supreme Court held Great Western liable for its failure to exercise reasonable care in protecting the buyers from construction defects. The court imposed tort liability on the lender because the lender knew of the developer’s undercapitalization and inexperience, thus making it reasonably foreseeable that the developer would cut corners in its construction of the homes.

In response to Connor, California enacted legislation that restricted lender liability to circumstances in which construction defects were a direct or proximate result of the lender’s nonlending activities and misrepresentations. Other jurisdictions appear to follow California by “limiting the liability of lenders to situations in which they have become in essence joint venturers.” In Terrace Condominium Ass’n v. Midlantic National Bank, the New Jersey Superior Court held that a lender that took title to a condominium in lieu of foreclosure and subsequently finished construction on the units was subject to implied warranty liability. Because the lender held itself out to the public as a builder-vendor, the court rejected its defense that it was merely a “mortgagee-in-possession.” Accordingly, the court held,

[S]ince Midlantic took over construction, it must be held to have assumed all of the obligations and responsibilities of the initial builder and developer and to have become a full-fledged “builder-vendor,” responsible for all defects, including those beyond the scope of what it perceives to be its own limited construction activities.

57. Id. at 616.
58. Id. at 619–20.
59. Id. at 611.
60. Id. at 617 (applying a six-part test espoused by the California Supreme Court ten years prior in Biakanja v. Irving, 320 P.2d 16, 19 (Cal. 1958)).
61. Id. at 617 (finding the “onerous” burden of the loans aggravated the financial situation of the developer).
62. Id.
63. See KNAPP, CRYSTAL & PRINCE, supra note 23, at 505 (citing CAL. CIV. CODE § 3434 (West 1997)); Webb, supra note 24, at 511 (citing CAL. CIV. CODE § 3434).
64. Webb, supra note 24, at 512.
65. KNAPP, CRYSTAL & PRINCE, supra note 23, at 505.
67. Id. at 1062–64.
68. Id. at 1064 (internal quotation marks omitted).
69. Id. at 1065.
2. *South Carolina: Early Lender Liability*

In early South Carolina cases involving implied warranties, the supreme court focused liability on the builder and the vendor;\(^7^0\) in later decisions, the court expanded liability to lenders.\(^7^1\) In *Roundtree Villas Ass’n v. 4701 Kings Corp.*,\(^7^2\) a purchaser brought a construction defects action against a lender under a theory of implied warranty.\(^7^3\) The lender created a corporation to sell housing units, and the builder subsequently deeded the remaining unsold units to this corporation, which sold the units.\(^7^4\) After numerous complaints regarding the roofs and balconies in the units, and in an effort to increase the marketability of the remaining unsold units, the lender hired an inspection team to determine the extent of the repairs needed.\(^7^5\) Instead of adopting a more costly method that would remedy the problem, the lender opted for a temporary solution.\(^7^6\) When the problem persisted, the purchasers brought an action against the lender for a breach of an implied warranty.\(^7^7\) In rejecting the extension of liability to a lender for construction defects, the court noted that an implied warranty is effectively a contract; because the record was devoid of facts indicating the presence of a contractual agreement between the lender and purchasers, liability did not extend to the lender.\(^7^8\)

Five years later, in *Kennedy v. Columbia Lumber & Manufacturing Co.*,\(^7^9\) the court recognized the potential liability under the implied warranty of habitability for a lender that has a substantial involvement in the construction of a home.\(^8^0\) Columbia Lumber supplied materials to a builder for the construction of a home.\(^8^1\) After substantially completing the house, the builder encountered difficulty in repaying its loans to Columbia Lumber.\(^8^2\) Instead of foreclosing on its mechanics lien on the property, Columbia Lumber took title to the home and subsequently sold the home to Kennedy.\(^8^3\) Six years later, Kennedy discovered a crack in the brick veneer, and inspections revealed that a faulty foundation caused the crack.\(^8^4\)

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73. See id. at 423, 321 S.E.2d at 51.

74. Id. at 419–20, 321 S.E.2d at 49.

75. Id. at 420, 321 S.E.2d at 49.

76. Id.

77. Id. at 418, 321 S.E.2d at 48.

78. Id. at 423, 321 S.E.2d at 51.


80. Id. at 341, 384 S.E.2d at 734.

81. Id. at 338, 384 S.E.2d at 732.

82. Id.

83. Id. at 338, 384 S.E.2d at 732–33.

84. Id. at 338, 384 S.E.2d at 733.
Kennedy then brought a claim against Columbia Lumber for a breach of the implied warranty of habitability. In discussing whether Columbia Lumber would be liable in this situation, the court outlined various scenarios that imposed liability upon lenders: where the lender is also the developer; where the lender knowingly makes false, express representations to a buyer; where the lender is in essence a joint venturer; where the lender’s business is so intertwined with the builder’s so as to obscure the legal distinctions between the two; and in the peculiar instance where a lender “forecloses on a developer in the midst of construction, takes title, has substantial involvement in completing the construction,” and then sells the home itself. However, because Columbia Lumber did not act in any of these capacities, the court did not hold the company liable under the implied warranty of habitability.

III. *Kirkman v. Parex, Inc.*

In *Kirkman v. Parex, Inc.*, the court revisited the test of substantial involvement espoused in *Kennedy*. The Kirkmans entered into a contract for the sale of a home with Miller Housing Corporation. In turn, Miller Housing received financing from First Union to build the home. Before Miller Housing could complete the construction, financial difficulties arose that compelled First Union to foreclose on the loan. First Union hired a contractor to finish the construction of the home, and upon completion of the house, the Kirkmans received a deed stating that the house was sold “as is” and disclaiming the implied warranty of habitability.

After the sale, the Kirkmans spent approximately $45,000 repairing defective artificial stucco on the exterior of the home. The Kirkmans then brought a claim for breach of the implied warranty of habitability against First Union as the seller of the property, alleging they were unaware of the “as is” provision and disclaimer within the deed for the house. The circuit court granted summary judgment in favor of First Union upon a finding that the bank was a mere lender and thus could not have impliedly warranted the habitability of the house. The court of appeals

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85. *Id.*
86. *Id.* at 340, 384 S.E.2d at 734.
87. *Id.*
88. *Id.*
89. *Id.*
90. *Id.* at 340-41, 384 S.E.2d at 734.
91. *Id.* at 341, 384 S.E.2d at 734.
93. See *Id.* at 483–85, 632 S.E.2d at 857–58.
94. *Id.* at 480, 632 S.E.2d at 855.
95. *Id.*
96. *Id.* at 480, 632 S.E.2d at 855–56.
97. *Id.* at 481, 632 S.E.2d at 856.
98. *Id.*
99. *Id.*
100. *Id.* at 481–82, 632 S.E.2d at 856.
affirmed, and the supreme court granted the Kirkmans’ petition for a writ of certiorari.

The South Carolina Supreme Court rejected the trial court’s and appellate court’s determination that First Union was a mere lender and held that there remained “a genuine issue of material fact whether First Union was substantially involved in completing the construction” of the home. The court then noted that if, on remand, First Union is found to have been substantially involved without having disclaimed liability, it impliedly warranted the habitability of the home. Thus, upon a finding of substantial involvement, the lower court must next determine if First Union effectively disclaimed the warranty. While the requirements for a disclaimer are stringent, they would relieve First Union of liability if met. However, if the fact finder determines that First Union was substantially involved and did not disclaim the implied warranty, the lower court should then conduct a determination as to whether First Union breached the implied warranty.

Kirkman signals the potential for lender liability in accordance with the court’s historic adherence to caveat venditor. However, as discussed in Parts IV and V, the test of substantial involvement and the specifically-bargained-for element of effective disclaimers leave lenders uncertain about how to avoid liability for a breach of implied warranty.

IV. SUBSTANTIAL INVOLVEMENT REQUIREMENT FOR LENDER LIABILITY AS A BASIS OF THE IMPLIED WARRANTY OF HABITABILITY

The South Carolina Supreme Court’s decision to reverse Kirkman and remand the case to the circuit court signals the emergence of potential lender liability in contract under the implied warranty of habitability. This extension of liability is consistent with other jurisdictions’ imposition of liability on a lender who partakes in nonlender activity and is sound as a matter of public policy because it affords buyers greater protection. Yet, in its attempt to adhere to the doctrine of caveat venditor, the court has left lenders uncertain as to what specific actions constitute substantial involvement. Uncertain about what actions qualify as substantial involvement, lenders remain uncertain about the type of actions that could expose them to liability under the implied warranty of habitability.

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101. ld. at 482, 632 S.E.2d at 856.
102. ld. at 480, 632 S.E.2d at 855.
103. ld. at 483–84, 632 S.E.2d at 857.
104. ld. at 485, 632 S.E.2d at 858.
105. Id. 632 S.E.2d at 859.
106. Id.
107. See id. (“We adopt the requirements set forth by the Washington Court of Appeals: the disclaimer ‘must be (1) conspicuous, (2) known to the buyer, and (3) specifically bargained for.’” (quoting Burbo v. Harley C. Douglass, Inc., 106 P.3d 258, 263 (Wash. Ct. App. 2005))).
108. Id.
109. See supra text accompanying notes 24–53.
110. See discussion supra Part II.B.1.
In *Kennedy v. Columbia Lumber & Manufacturing Co.*, the court refused to impose implied warranty liability on a mere lender but recognized potential lender liability in certain situations. Specifically, the *Kennedy* court noted,

[A] lender can be held liable if it is also a developer. . . . Liability may also attach when the lender becomes highly involved with construction in a manner that is not normal commercial practice for a lender. In such a situation, the lender might be said to be a joint venturer. The lender may be liable if it is so amalgamated with the developer or builder so as to blur its legal distinction. A lender may also be liable where it forecloses on a developer in the midst of construction, takes title, has substantial involvement in completing the construction and sells homes.

Thus, the court’s separation of a developer, joint venturer, or amalgamate from the substantial involvement situation indicates that this fourth category is distinct from the other three situations; however, it leaves lenders uncertain as to when their conduct will fit within this distinct category.

Prior caselaw illustrates scenarios of lender liability in the context of developers, joint venturers, or amalgamated lenders but does not provide a fact pattern in which a lender was substantially involved. Apparently, a lender is considered a developer when it is also involved in the development of the home sold to the purchasers. Similarly, a lender is presumably a joint venturer when the lender has an equity ownership in the project with another entity. Likewise, a lender is deemed to be amalgamated if it merges with a developer or builder so as to appear to be a united entity.

Thus, lenders can be reasonably certain as to when they will fall into these categories and be subject to implied warranty liability; however, they are left with uncertainty in predicting what actions will subject them to liability for being substantially involved. In its articulation of this test, the *Kirkman* court held that an affirmative finding of substantial involvement is not based on whether the lender was responsible for installation of the defective portion of the new home but instead involves a question of fact for a jury. However, the court’s failure to

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112. See id. at 340–41, 384 S.E.2d at 734.
113. Id. at 340–41, 384 S.E.2d at 734 (internal citations omitted).
114. See, e.g., Lane v. Trenholm Bldg. Co., 267 S.C. 497, 499–501, 229 S.E.2d 728, 729 (1976) (discussing facts in which a lender was also a developer).
115. See, e.g., Cent. Bank, N.A. v. Baldwin, 583 P.2d 1087, 1088–89 (Nev. 1978) (finding that a bank’s subsidiary’s ownership of half the stock of a developer, in addition to overtures on behalf of the subsidiary towards the developer, necessitated a finding of a joint venturer).
116. See, e.g., Kineaid v. Landing Dev. Corp., 289 S.C. 89, 96, 344 S.E.2d 869, 874 (Ct. App. 1986) (finding that the cross-ownership of all parties concerned in the development required the court to decide the lender was amalgamated with the seller).
118. See id. at 340, 384 S.E.2d at 734.
119. See id. at 340–41, 384 S.E.2d at 734.
121. Id. at 485, 632 S.E.2d at 858.
outline factors tending to support or reject a finding of substantial involvement compounds lender uncertainty.

As stated in Kirkman, if a trier of fact determines a lender is substantially involved in completing the construction of a new home, then the lender is held to have impliedly warranted the dwelling.\textsuperscript{122} Accordingly, without a clear definition of what constitutes substantial involvement, lenders likely will begin attempting to disclaim the implied warranty of habitability for property they sell to avoid this uncertainty. But, even if lenders attempt to place a disclaimer in every sales contract, they must still determine if their disclaimer will be effective.

V. DISCLAIMERS OF THE IMPLIED WARRANTY OF HABITABILITY BY FINANCIAL INSTITUTIONS IN SOUTH CAROLINA

The prevailing view is that sellers may disclaim the implied warranty of habitability.\textsuperscript{123} In Kirkman, the South Carolina Supreme Court agreed with the Washington court’s requirements for a valid disclaimer of this warranty: a seller’s disclaimer of the implied warranty “must be (1) conspicuous, (2) known to the buyer, and (3) specifically bargained for.”\textsuperscript{124} The court in Kirkman mandated a strict application of these three prongs and indicated that fulfillment of these requirements will only be met in rare circumstances.\textsuperscript{125} Additionally, whether each requirement is satisfied is a jury issue that can be supported or contradicted by extrinsic evidence.\textsuperscript{126} Based on caselaw, the first two requirements apparently will easily be fulfilled with a standard form and initialing requirement;\textsuperscript{127} however, how the seller will prove satisfaction of the third element remains unclear.\textsuperscript{128}

A. Conspicuous: Caselaw

While the Uniform Commercial Code (UCC) does not apply to the implied warranty of habitability,\textsuperscript{129} South Carolina courts have extended its application to non-UCC cases for guidance in determining whether a disclaimer is conspicuous.\textsuperscript{130} South Carolina’s codified version of the UCC’s definition of conspicuous\textsuperscript{131} states that a clause is considered conspicuous “when it is so written that a reasonable

\textsuperscript{122} Id.
\textsuperscript{123} Knapp, Crystal & Prince, supra note 23, at 503; see also Kirkman, 369 S.C. at 485, 632 S.E.2d at 858 (agreeing with the stance of the Alabama Supreme Court “that the principle of freedom of contract permits a party to effectively disclaim the implied warranty of habitability” (quoting Turner v. Westhampton Court, L.L.C., 903 So. 2d 82, 93 (Ala. 2004)) (internal quotation marks omitted)).
\textsuperscript{125} Id.
\textsuperscript{126} See id. at 485–86, 632 S.E.2d at 858.
\textsuperscript{127} See infra notes 128–50 and accompanying text.
\textsuperscript{128} See Burbo, 106 P.3d at 263 (concluding summarily that an attempted disclaimer “was not negotiated”); Bridges v. Ferrell, 685 P.2d 409, 411 (Okla. Civ. App. 1984) (recognizing that disclaimers of the implied warranty of habitability “are strictly construed against the builder-vendor”).
person against whom it is to operate ought to have noticed it.’’\textsuperscript{132} The statute states that a disclaimer is conspicuous if it has a printed heading in capital letters or if the language is larger or of a contrasting type or color than the rest of the print in the form document.\textsuperscript{133}

In \textit{Nettles v. Techplan Corp.},\textsuperscript{134} the United States District Court for the District of South Carolina emphasized the location of the disclaimer and granted summary judgment for an employer even though the clause in question was not in bold or contrasting type or of a different color.\textsuperscript{135} As outlined by the court,

\begin{quote}
South Carolina cases applying the UCC definition of “conspicuous” consistently consider three factors in determining whether a certain disclaimer is or is not conspicuous. First, the courts consider the type-setting of the disclaimer, i.e. if the disclaimer is in the same type as the remainder of the agreement containing the disclaimer. Second, the courts have looked to the color of the print in which the disclaimer is written. Finally, the courts consider the location of the disclaimer within the document or contract.\textsuperscript{136}
\end{quote}

The court held that the positioning of the disclaimer on the first page of the manual was “sufficiently conspicuous such that a reasonable person against whom it is to operate ought to have noticed it.”\textsuperscript{137} However, in \textit{South Carolina Electric \& Gas Co. v. Combustion Engineering, Inc.},\textsuperscript{138} the South Carolina Court of Appeals held that a disclaimer not set apart from the text by color or type and located seventeen pages into a twenty-two page single spaced document was not conspicuous.\textsuperscript{139} Moreover, in a case where the language of a disclaimer was in all capital letters, the court of appeals found a genuine issue of material fact as to whether the clause was conspicuous because it was not underlined or set apart by a contrasting type or color.\textsuperscript{140} These holdings illustrate the myriad of factors—sometimes dispositive, sometimes not—courts may consider in determining the issue of conspicuousness, none of which appear to be outcome determinative.\textsuperscript{141}

\textsuperscript{132} \textit{Id.}
\textsuperscript{133} \textit{Id.}
\textsuperscript{134} 704 F. Supp. 95 (D.S.C. 1988).
\textsuperscript{135} \textit{Id.} at 98.
\textsuperscript{136} \textit{Id.}
\textsuperscript{137} \textit{Id.}
\textsuperscript{139} \textit{Id.} at 186, 322 S.E.2d at 456.
\textsuperscript{141} \textit{See Myrtle Beach Pipeline.}, 843 F. Supp. at 1038. The court concluded that the various factors to be considered by a court in determining whether a document is conspicuous for purposes of disclaiming an implied warranty pursuant to section 36-2-316(2) of the South Carolina Code include the following:

\begin{enumerate}
\item the color of print in which the purported disclaimer appears;
\item the style of print in which the disclaimer is written;
\item the size of the disclaiming language, particularly in relation to other print in the document;
\item the location of the disclaimer in the contract;
\item the appearance of the term “merchantability” with
A paradigmatic case in which a disclaimer would clearly be conspicuous would be one in which the party intending to disclaim differentiated the disclaimer by size, font, and color.\textsuperscript{142} Where an employer placed a disclaimer on the cover of an employment manual, on a separate page of the handbook, and typed the disclaimer in a larger font than the rest of the text, the court held the disclaimer to be conspicuous.\textsuperscript{143} Thus, it appears that a lender could successfully meet the “conspicuous” requirement by clearly labeling the disclaimer in differing font, size, or color from that used in the sales contract.

B. Known to the Buyer

South Carolina Code section 36-1-201(10) provides that for a disclaimer to be conspicuous it should be written so that a reasonable person ought to notice it.\textsuperscript{144} However, Kirkman’s second requirement that the disclaimer be “known to the buyer” presents a more stringent standard than that set forth in the UCC; the rule announced by the supreme court requires actual knowledge\textsuperscript{145} as compared to the less rigid UCC standard that a reasonable person “ought to have noticed” the disclaimer.\textsuperscript{146} Because of this more stringent standard, lenders are now left with the burden of proof in demonstrating that the disclaimer was known to the buyer.

In Breckenridge v. Cambridge Homes, Inc.,\textsuperscript{147} the Appellate Court of Illinois denied the buyers’ claim for breach of the implied warranty of habitability based on the finding that one of the buyers initialed in the margin next to the disclaimer language in the sales contract.\textsuperscript{148} Because the buyers were educated and experienced business people who chose to initial the contract after reading it, the court held that this action signaled their acceptance of the terms of the disclaimer.\textsuperscript{149} In addition to emphasizing the presence of the buyers’ initials, the court also examined testimony of the buyers’ conversation with the sales agent in which the buyers stated that they understood that placing their initials on the contract signaled their understanding of the implications of the disclaimer.\textsuperscript{150} As a result of these factual findings, the court concluded that the buyers were put on notice of the disclaiming

\begin{itemize}
\item respect to color, style, size, and type of print in the disclaimer clause; and
\item the status of the parties contesting the validity of the disclaimer, namely whether they be consumers or commercially sophisticated entities. While these factors lend aid to the determination of what constitutes “conspicuous” language, the court believes that no single factor is dispositive nor are these enumerated factors exhaustive of all the criteria that can be used in examining a disclaimer.
\end{itemize}

\textit{id.} (citing S.C. CODE ANN. § 36-2-316(2) (2003)).

\textsuperscript{142} See S.C. CODE ANN. § 36-1-201(10); Kumpf v. United Tel. Co. of the Carolinas, 311 S.C. 533, 538, 429 S.E.2d 869, 872 (Ct. App. 1993) (holding that the absence of factors such as color, font, and a distinctive border calling attention to the disclaimer supported the decision that it was not conspicuous).


\textsuperscript{144} S.C. CODE ANN. § 36-1-201(10).


\textsuperscript{146} S.C. CODE ANN. § 36-1-201(10).

\textsuperscript{147} 616 N.E.2d 615 (Ill. App. Ct. 1993).

\textsuperscript{148} id. at 620.

\textsuperscript{149} Id.

\textsuperscript{150} Id.
language and had waived their right to claim a breach of the implied warranty of habitability. 151

Thus, it appears that one way a lender will satisfy the “conspicuous” and “known to the buyer” requirements is through the creation of a standard disclaimer form. Both elements can be satisfied by creating a separate section clearly labeled “Disclaimer of the Implied Warranty of Habitability” that is in a type differing in size, color, or font from the original sales contract and that requires the buyer to acknowledge his acceptance of its terms. Apparently, this requirement would be fulfilled by having a buyer initial beside the disclaimer, indicating that the buyer acknowledged, read, and understood the ramifications of the disclaimer. However, lenders likely will face uncertainty in determining whether the disclaimer was specifically bargained for.

C. Specifically Bargained For

The UCC recognizes a bargaining element present in sales transactions that is useful in attempting to determine the meaning of the third prong of the disclaimer test—whether the seller specifically bargained for the disclaimer. 152 As stated in the South Carolina Reporter’s Comments to South Carolina Code section 38-2-316, 153 the statute aims to protect a buyer from receiving a product the buyer did not bargain for while still affording the seller an opportunity to expressly disclaim implied warranty obligations. 154 However, because the UCC does not mandate negotiation of a disclaimer, Kirkman presents lenders with a stricter standard of proving a disclaimer was specifically bargained for in negotiations between the buyer and seller. 155 Lenders will face uncertainty in determining how to meet this standard as there is a lack of caselaw illustrating the types of factors that would fulfill this requirement. Other jurisdictions, however, have addressed the issue.

A California court has held a disclaimer is not specifically bargained for if it is given to the buyer after the sale is complete. 156 The court reasoned that a buyer cannot bargain for the implications of a disclaimer of implied warranties, or the limitations that accompany this waiver, if the disclaimer is not presented to the buyer until after the sale. 157 In addition to this factor, lenders may also look to Kirkman, which suggests the price reduction of a home as an example of a desired

151. Id.
154. Id.
155. See Kirkman, 369 S.C. at 485, 632 S.E.2d at 858 (quoting Burbo, 106 P.3d at 262) (internal quotation marks omitted).
157. See id. at 523 (quoting Rehurek v. Chrysler Credit Corp., 262 So. 2d 452, 455 (Fla. Dist. Ct. App. 1972)); Sanco, Inc. v. Ford Motor Co., 771 F.2d 1081, 1086 (7th Cir. 1985) (“[A]s a general proposition, a seller may not ‘spring’ a warranty disclaimer on a customer after a sale has been consummated; the parties must have understood that . . . any disclaimers . . . were part of their deal.”).
benefit a buyer would exchange for knowingly disclaiming the protection of the implied warranty of habitability.\footnote{158}{See Kirkman, 369 S.C. at 485, 632 S.E.2d at 858 (“[The three-part disclaimer test] will protect buyers but also give them freedom to purposefully bargain for a price discount or other desired benefit.”).}

However, aside from a basic prohibition against imposing disclaimers on buyers after the completion of a sale and price reduction, little guidance exists that illustrates how a lender may prove that the seller specifically bargained for the disclainer. Thus, there will remain much uncertainty on the part of lenders in discovering what factors will be indicative of proving fulfillment of this requirement. This uncertainty of the specifically-bargained-for element coupled with the uncertainty of the substantial-involvement test supports use of an alternative method by which lenders can avoid implied warranty liability while still affording the buyer protection from latent defects.

\section{VI. A Suggestion Following the Kirkman Decision: Legislation Allowing a Lender or Developer to Obtain Additional Insurance}

\textit{Kirkman} is sound as a matter of policy because it seeks to ensure that buyers receive the benefit of their bargain by imposing liability for construction defects on lenders who were substantially involved in the construction; such lenders are better situated to avoid construction defects. However, because lenders likely will incur substantial difficulty in determining what constitutes substantial involvement and in proving that the seller specifically bargained for a disclaimer, this section discusses a legislative alternative whereby additional insurance could be acquired by the lender or developer. Such insurance would be obtained in lieu of disclaiming the implied warranty of habitability and would coincide with the policy of affording the buyer of a new home protection from latent defects.

\textit{A. Policy Implications of the Kirkman Decision: General Policy Behind Caveat Venditor}

Because \textit{caveat venditor} is premised “on the just philosophy that a sound price warrants a sound commodity,”\footnote{159}{Lane v. Trenholm Bldg. Co., 267 S.C. 497, 502, 229 S.E.2d 728, 730 (1976) (internal quotation marks omitted).} it follows that when buyers pay a fair price for a new home they should receive what they bargained for—a home suitable for habitation.\footnote{160}{See id. at 503, 229 S.E.2d at 730–31.} Expecting a buyer to give up a large amount of money for the purchase of a new home\footnote{161}{See id. at 503, 229 S.E.2d at 731 (stating that the purchase of a home likely involves the investment of the buyer’s life savings and a mortgage); Comment, Liability of the Institutional Lender for Structural Defects in New Housing, 35 U. Chi. L. Rev. 739, 753 (1968) (“Buying a home is generally the largest investment a family ever makes.”).} without receiving adequate compensation in the form of a habitable dwelling and protection from latent defects would contradict public policy.\footnote{162}{Lane, 267 S.C. at 503, 229 S.E.2d at 731.} The implied warranty of habitability is one of three implied warranties...
recognized within construction law in South Carolina. The recognition of three implied warranties illustrates the desire of South Carolina courts to protect a purchaser from latent defects. Because the primary purpose of a home sale is to provide a buyer with a home that is suitable for habitation, the innocent purchaser is forced to rely on the builder who holds itself out to be an expert in construction. Thus, the emergence and adoption of caveat venditor in South Carolina serves to afford innocent buyers greater protection from latent defects in a transaction in which they are unfamiliar with construction techniques and must rely on the expertise of builders.

B. Policy of Lender Liability

The rationale supporting builder-vendor liability under the implied warranty of habitability is that buyers have an unequal bargaining position in relation to sellers. The potential for lender liability under the implied warranty shifts the responsibility of ensuring that the home is free from latent defects to lenders that are substantially involved in the construction of a home. This shift of potential liability results from the fact that purchasers cannot readily discover latent defects because of such factors as the average buyer’s unfamiliarity with construction and the expense of hiring an inspector.

Where a lender goes beyond the normal role of a mere lender and is concurrently a developer, joint venturer, or has substantial involvement in the completion of the home, that lender may be subjected to implied warranty liability similar to that of a builder-vendor. Such imposition of liability affords buyers greater assurance and fulfills the reasonable expectations of those contemplating the use of the home as a dwelling for their families. Moreover, extension of implied warranty liability to lenders provides purchasers with a remedy where a builder lacks the financial resources to cure a construction defect. Hence, when compared with an innocent purchaser, lenders are in a better position to avoid such construction defects and, through the potential imposition of liability, have incentive to prevent the faulty construction of a home.

The Kirkman decision ensures that when a lender places a home in the stream of commerce by selling it to a buyer for a fair price, the buyer’s bargain for a

163. LAWRENCE C. MELTON, SOUTH CAROLINA CONSTRUCTION LAW 352–53 (2005) (listing the three implied warranties recognized in South Carolina construction law as the following: (1) the “[i]mplied warranty that plans and specifications are sufficient ‘for the purpose in view’”; (2) the “[b]uilder’s [i]mplied warranty of workmanlike service”; and (3) the “[s]eller’s [i]mplied warranty of fitness and habitability”).

164. See id. at 351 (“Implied warranties are created by law to protect the purchaser from latent defects.”).


167. Id. at 413–14, 175 S.E.2d at 795.

168. See Terlinde v. Neely, 275 S.C. 395, 398, 271 S.E.2d 768, 769 (1980) (“[T]he character of society has changed such that the ordinary buyer is not in a position to discover hidden defects in a structure, especially at a time when he is provided more elaborate furnishings which tend to obscure the structural integrity of the facility.”); Rutledge, 254 S.C. at 411, 175 S.E.2d at 794 (noting that a prospective purchaser would not be able to discover whether a sewer system was properly installed).

Habitable dwelling is protected. Thus, Kirkman is sound as a matter of policy because it imposes liability on lenders that are substantially involved in the building of a house, unless the lenders effectively disclaim the implied warranty and, in exchange, the buyers receive a negotiated discount or other "desired benefit." However, as discussed previously, the holding creates two uncertainties: what constitutes substantial involvement and when a disclaimer is specifically bargained for. Such uncertainties on the part of lenders are bound to lead to an increase in lending costs. Accordingly, the Kirkman decision leaves unanswered the question of whether there is a way to obtain the policy benefits of imposing implied warranty liability on lenders without increasing the costs associated with the sale of a home.

C. Potential Legislation

While the policy implications of Kirkman are sound, the uncertainty presented to lenders by this decision is substantial. Moreover, courts are likely to construe disclaimers in favor of the buyer, exacerbating the troubles lenders will have with determining how to effectively protect themselves. One way to deal with the costs of these uncertainties is for the South Carolina legislature to offer a possible alternative to the framework presented in Kirkman. Such an alternative would allow lenders who provide or arrange for adequate insurance in the event of construction defects to be relieved of implied warranty liability. This type of insurance would protect innocent purchasers from construction defects while simultaneously reducing uncertainty for lenders.

Accordingly, the proposed alternative solution of this Note is the implementation of legislation requiring lenders or their developers to offer additional insurance if they disclaim the implied warranty of habitability. The determination of the type and quantity of coverage deemed to constitute adequate insurance would be defined either by a statute or by a rule promulgated by an appropriate agency. For example, adequate insurance could be defined as the full replacement value of the home as defined by the Insurance Commission. Such legislation would provide a statutory safe harbor for lenders by giving them the option to avoid liability as long as the lender carries adequate insurance. This would effectively relieve lenders of claims under the implied warranty of habitability, while continuing to afford buyers protection from latent construction defects. Theoretically, application of this alternative to cases like Kirkman would create cost spreading; the cost of acquiring additional insurance to cover damages arising from latent defects would be passed on from the lender or developer to the buyer through

171. See discussion supra Parts IV–V.
172. See Kirkman, at 485, 632 S.E.2d at 858 ("The three-part disclaimer test is to be applied strictly and will be met only in rare circumstances.").
173. The proposed legislative solution of this Note is similar to an insurance proposal set forth previously. See Comment, supra note 161, at 753 ("The loan association could force builder-vendors to insure against ‘products liability’ as a condition to receipt of a construction loan, thereby reducing or even eliminating the occasions where purchasers would seek redress from the association.").
an increase in the purchase price of the home.\textsuperscript{174} Additionally, this alternative creates less potential for litigation costs while still adhering to the doctrine of \textit{caveat venditor}.

\textbf{D. Cost-Benefit Analysis}

Ultimately, the lender’s decision between utilizing a disclaimer and acquiring additional insurance would be based on which legal regime best minimizes the lender’s construction loan transactions. Because lenders are likely in the best position to judge the market, they will be able to determine which option is best suited for their needs. Where lenders opt to disclaim potential warranty liability, they are faced with potential liability and litigation costs flowing from the judicial determination of whether they were substantially involved in the construction and whether they executed an enforceable disclaimer.\textsuperscript{175} Presumably, if lenders face greater liability and litigation costs, they will effectively pass these additional costs on to the consumers by including them in their rate structure. The benefit of this option to buyers is that they receive protection against construction defects from a builder or lender, provided the lender is found to have not adequately disclaimed the implied warranty.\textsuperscript{176} However, whether a disclaimer is effective is subject to judicial determination; thus, protection for buyers against latent defects is subject to the risks of litigation—some buyers will receive protection and others will not.

Additionally, a disclaimer presents consumers and lenders with great potential for substantial litigation costs. Such costs would arise under the method presented in \textit{Kirkman}—both a lender and buyer will first face judicial determinations of whether the lender was substantially involved in the construction and whether the lender successfully disclaimed the implied warranty of habitability.\textsuperscript{177} Assuming the court answers in the affirmative to the former but not the latter, the court would next have to decide whether an actual breach of the implied warranty had in fact occurred and determine the proper damages to award the buyer if such a breach occurred.\textsuperscript{178} This potential problem is compounded by the uncertainty as to whether the lender will be liable to the buyer for litigation costs in the event of a finding for the buyer.

If South Carolina provides an alternative under which lenders have the option to provide insurance and thereby opt out of liability, consumers will be protected in accordance with \textit{caveat venditor}, and lenders would exchange the litigation costs connected with the enforceability of a disclaimer for the cost of insurance. Presumably, the increased cost of insurance for lenders would be passed on to buyers; however, this likely would not be any greater than that currently passed on to buyers because of litigation costs under the disclaimer method. Alternately, the lender could require the developer to obtain insurance protecting against such

\textsuperscript{174} See Comment, \textit{Indirect Liabilities of Construction Lenders in a Development Setting}, 127 U. PA. L. REV. 1525, 1562 (1979) (“[C]onstruction lenders are in a position to reduce the risks and spread the costs of liability... [The lender spreads the cost] by passing the cost of insurance on to builders and ultimately consumers...”).

\textsuperscript{175} See \textit{Kirkman}, 369 S.C. at 486, 632 S.E.2d at 858.

\textsuperscript{176} See \textit{id.} at 485, 632 S.E.2d at 858.

\textsuperscript{177} See \textit{id.} at 486, 632 S.E.2d at 858.

\textsuperscript{178} See \textit{id.} at 485–86, 632 S.E.2d at 858.
defects before agreeing to grant the developer loans. Regardless of whether the additional cost of insurance is incurred through increased lending rates or by a requirement from the lender, the developer could still pass on the cost of insurance to buyers through an increase in the purchase price.

If the lender chooses to obtain the insurance in lieu of disclaiming the implied warranty of habitability, this cost could effectively be passed on to builders through an increase in lending rates. In requiring higher rates on loans, lenders may examine developer-borrowers more conservatively, thereby creating the additional burdens of time and cost of screening upon the lender. However, any additional cost incurred by the lender could be effectively passed along to the buyer through an increase in loan rates. It follows that a more conservative screening process likely would have a greater impact on smaller, less financially-stable developers than on those with greater financial stability. An obvious downside to this type of market impact is that such domination over the development market could weaken the price competition within the industry, therefore, buyers could potentially be driven out of the market by an increase in housing prices.

However, as mortgages are typically paid off in monthly installments over multiple years, even significant price inflation likely would not drastically increase monthly payments; thus, the likelihood of driving consumers out of the market would not be considerable. Additionally, while such screening could drive smaller, less financially stable developers out of the market, consumers may be willing to pay more for homes built by developers who have passed the elevated tests of the lenders. Such recognition by the lender as being financially sound would naturally elevate the reputation of a developer and be appealing to buyers making such a major purchase, thus serving as justification for paying an increased price in housing.

While arguably the buyer is effectively paying for the cost of litigation of both successful and unmeritorious claims that may not be the buyer’s claims, this cost should be weighed against the risk and potential cost the buyer would incur if faced with bringing a suit against the lender. As lenders or developers would merely file claims with their respective insurance carriers to settle claims for latent defects, parties would only be presented with court costs when a dispute arose as to damage amounts. Thus, this legislative alternative would benefit consumers as protection

179. See Comment, supra note 174, at 1562.
180. See id. at 1562–63.
181. See id. at 1563.
182. See Comment, supra note 161, at 755.
183. Such additional insurance would serve as a “signaling” device similar to those discussed in Jeff Sovrn, Toward a Theory of Warranties in Sales of New Homes: Housing the Implied Warranty Advocates, Law and Economics Mavens, and Consumer Psychologists Under One Roof, 1993 Wis. L. Rev. 13, 69 (1993). Specifically, Professor Sovrn stated:

"Signaling theorists contend that consumers interpret warranties as statements about the quality of the item warranted. Manufacturers who sell more reliable products may offer better warranties at less cost than manufacturers who sell goods of lower quality; therefore, the theory goes, consumers who [want] more reliable products should search for the best warranty coverage."

Id.

184. See Comment, supra note 161, at 754 (“Those increased construction costs... pass[ed] on to home purchasers in the form of higher prices will spread the costs of compensating victims of construction defects among all purchasers.”).
would be ensured by an increase in price—perhaps through monthly mortgage payments—as compared to the potential large, one-time sum for litigation that may or may not result favorably for the buyer.

In examining the two alternatives, the question becomes, “Which is the more cost effective option?” Because lenders are in the best position to make this determination, the adoption of the legislative alternative will allow them to implement the method that is most efficient. In either system, buyers will receive protection from latent construction defects while lenders can choose the alternative that is better suited for each transaction. However, the legislative alternative presented above is probably the superior solution because it assures buyers greater protection from latent construction defects and decreases potential litigation costs for lenders.

VII. CONCLUSION

While the Kirkman decision is sound as a matter of policy in its adherence to caveat venditor, lenders likely will be left with uncertainty as to how to determine what constitutes substantial involvement and how to prove that a disclaimer was specifically bargained for. Without proper guidance, attempts on the part of lenders to disclaim implied warranty liability likely will be the source of much litigation. Accordingly, in an effort to maintain the protection of buyers from latent defects, the enactment of legislation allowing lenders or developers the option to acquire insurance in lieu of a disclaimer will avoid the uncertainty arising from the Kirkman decision and decrease potential litigation costs for both lenders and buyers.

Margaret N. Fox

185. For example, it may be that a lender has confidence in a specific developer and chances litigation costs in lieu of definite insurance costs. Alternatively, where a lender has less certainty in a developer’s skill it may decide to acquire additional insurance.