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Fraud and Nondisclosure in the Vendor-Purchaser Relation*

By William B. Goldfarb

INTRODUCTION: ANALYSIS OF THE GENERAL PROBLEM

FEW CONCEPTS in the law of torts are more pervasive than the concept of misrepresentation. In many relationships, in many types of transactions, in many contexts and factual patterns—it is deemed an actionable wrong to misrepresent the facts to another. So universal is this idea that the term “fraud” has become a common mark of opprobrium for a person who is guilty of this wrong, for the scheme or device by which he perpetrates it and for his conduct in implementing his guilty design.

And yet, despite the hoariness of the fraud concept and the universality of its application, few subjects in the law are so confused and uncertain, so

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freighted with unanswered queries, so laden with inconsistencies.

Despite this confusion, certain broad propositions

emerge. One such proposition is that misrepresentation involves an activity. Typically, that activity consists of representing affirmatively, by means of *words*, that some fact¹ exists or does not exist. Certainly, when one thinks of fraud and deceit, one customarily conceives of it in such terms. But the affirmative act may be nonverbal. There flows through our law the idea that nonverbal conduct may be the equivalent of words and involve the same implications and legal effect. So, for example, contracts may be express or implied-in-fact. There would appear to be no reason why the existence or nonexistence of a fact cannot be represented by means of conduct as much as by means of words.

The most common type of nonverbal misrepresentation takes the form of concealment or disguise. For example, the defendant-seller covers a

* This article received first prize in the 1956 Sindell Tort Competition, awarded by Sindell, Sindell and Bourne.

¹ I do not intend to discuss the important but — for my purposes — irrelevant, problem of the misrepresentation of opinions or of intentions and the characterization of the state of one's mind as a representable, or misrepresentable, fact.

defect in his merchandise with a temporary patch, making it impossible for the plaintiff-buyer to notice it. The courts have not hesitated to hold that such conduct is tantamount to a verbal representation that the merchandise is free of defects.²

But instances of such misrepresentations are relatively rare. Basically, misrepresentation is a "*verbal tort*," like defamation, rather than an "*active tort*," like assault or false imprisonment.³ And the gravamen of the wrong is in the character of the false *words* used by the defendant and the reliance which they reasonably induce in the plaintiff, to his injury.

The question to be explored by this article is this: Under what circumstances does it constitute an actionable wrong for one to remain silent?

Silence taken alone is the most neutral of facts or states. But silence takes on the coloration of the surrounding circumstances, and may be pregnant with meaning.

The courts and commentators treat actionable silence or, as it is more often denominated, "actionable nondisclosure" as a variety of misrepresentation. It is one of the implied theses of the present inquiry that it is not logical, or even helpful, to do so. True, under some circumstances, a failure to speak may amount to the equivalent of an actual, verbal representation of fact. Silence is, after all, a type of conduct, or at least of forbearance. If the representation thus implied is, in fact, false, and if the other elements of fraud are present, the plaintiff ought to be entitled to a remedy. But, under many circumstances, silence is merely silence. It says nothing. The silent party may fail to deny or assert a given fact.

²In *Salzman v. Maldaver*, 315 Mich. 403, 24 N.W.2d 161 (1946), the seller of sheet aluminum wrapped in bundles, placed an undamaged sheet on top of each bundle for the purpose of concealing from the buyer the fact that the other sheets in the bundle were corroded. *Held*, actionable fraud.

In *Southern v. Floyd*, 89 Ga. App. 602, 80 S.E.2d 490 (1954) the vendor of a house not only failed to disclose to his purchaser that the furnace was defective but covered the break in the boiler of the furnace with a temporary filling and thereby prevented the plaintiff-purchaser, who exercised ordinary care, from discovering the defect. *Held*, the plaintiff could recover despite the fact that the contract of sale provided that it contained the entire contract and that no representation except as noted therein would be binding. This did not relieve the vendor.

Similarly, where a contract of sale of a house provided that there were no understandings except those contained therein, an action for damages was allowed, when it appeared that the vendor's agents knew that refinishing and painting had effectually concealed structural defects from the purchaser. Under the circumstances, the vendor's failure to reveal the hidden and material facts constituted fraud. *Herzog v. Capital Co.* 27 Cal.2d 349, 164 P.2d 8 (1945)

³The reason for this is not difficult to imagine. Man's intelligence is verbally-based. Our ideas are communicated and, possibly conceived in terms of words or symbols. Some have speculated whether "thought," in the sense in which we use the word, would even be possible in the absence of language.

But it may be unfair and unreasonable to label his behavior as a representation, much less a *misrepresentation*. And yet, even under such circumstances, the silence may be tortious.

The courts' insistence on relating such nondisclosure to misrepresentation seems to stem from a tradition of labeling and categorizing. It will avail us little to fight this tendency. It is enough to be aware of it. This awareness alone can help prevent us from falling prey to that most treacherous of semantic traps: the tyranny of labels.

The accepted theorem in this field may be summed up as follows: Silence or nondisclosure does not constitute an actionable wrong, unless the defendant is under a duty to speak and disclose. This is a distillation of the rule as it appears in countless decisions. It purports, in many cases, to be the ground of the decision, the *ratio decidendi*. But a little reflection will reveal that such a theorem can never be the ground or reason for any decision. It is far too general. And, it begs the question. The recitation of the purported "rule" naturally evokes the real question: *When is there a duty* to speak and to disclose? The "rule," as stated is not a reason, but rather a rationalization. Once the court imposes liability under the facts of a particular case, a duty is found to exist. And, conversely, once it is decided that the defendant, for whatever true "reasons," should not be held liable, it is "concluded" that there was no duty.

The emptiness of the "rule" and its artificiality as a basis of decision would be vividly demonstrated by using similarly broad and question-begging language in defining any tort or torts in general. Thus: one is guilty of tort because one breached his duty. The language used makes the statement sound like a "reason." But that presupposes that it were known, universally, and in a manner easily translatable into concrete application, when and whether the particular duty exists. But as to *this*, alas, there is no such recognized generalization or theorem.

The formula found in the decisions is that there is no duty to disclose unless there exists a fiduciary relationship between the parties, or other special circumstances. The first part of this "rule" has the ring of certainty and definiteness. But when one studies the cases, one comes reluctantly to the conclusion that this too is a rationalization rather than a reason. Apart from the standard or classical examples of fiduciary relations, the court is apt to find such a relationship when they have decided to hold the defendant liable. And if they are not inclined to find liability they conclude that there was no such relationship present. Of this, more later.

The second half of the proposition, that relating to "special circumstances," is, perhaps, a little more broadly stated than the *language* of the decisions warrants. But their *effect* is at least that flexible, and the rule

is patently formulated in such a manner as to enable it to fit the numerous situations which may or may not appeal to the conscience or ethical sense of the court.

In short the rule is not a rule. If there is a duty to disclose, then non-disclosure is tortious. This means, that if nondisclosure is for any reason damnable under the circumstances, there is a duty to disclose.

Where does this leave us? It leaves us in no worse a position than we would be in many other areas of the law. It is the old dilemma which Holmes so well summed up when he stated that the life of the law has not been logic, but experience.⁴ The only logic is the logic of experience, of history or of policy, i.e. a logic of goals and purposes rather than of reasons and rules. Students and practitioners of the law are left, then, to study the cases and to attempt to pierce the veil of language until the essence of the case is exposed, the truth whose relevance is to the facts and their import rather than to general propositions.

We proceed then to such an examination of the cases, in terms of a particular legal relation, viz. that between a vendor and a purchaser.⁵ It is always desirable to study a legal problem in terms of a relation. Within the framework of rights and duties which exist by virtue of the relation, it may be possible to draw some useful generalizations. Beyond the framework, generalization is hazardous.

The vendor-purchaser relation is one of the most important and most ubiquitous of all legal relations. It is the fundamental relation of the business world and a fertile area for tortious misrepresentation, by word, by act or by silence.

A word about the scope of this investigation. We are here concerned only with the substantive question: Is there a right of action? We are not concerned with the procedural question: What remedies are available? Sometimes the remedy will be a suit for money damages; sometimes it will be rescission. But whatever the desired remedy, the prior question arises: Is there a right? Or, in other words, was there a wrong?

I also assume all the formal elements of fraud where they may be prerequisite to recovery: scienter, materiality, falsity, intent to induce "reliance" and injury. Reliance is thus emphasized because it may be asked whether one relies on silence. In effect one may rely on appearances. But this is not the same, for silence does not always create an appearance. This question was discussed above in connection with the

⁴ HOLMES, *THE COMMON LAW* 1 (1881).

⁵ Properly, "vendor" and "purchaser" deal in real property, "buyer" and "seller" in personal property. Herein, I will follow the courts and not preserve the distinction. I will generally use the terms interchangeably, avoiding, moreover, except when quoting, the use of the term "vendee."

problem of whether or not nondisclosure always involves a representation.

Our inquiry then condenses to two questions:

1) Does a vendor have a duty to disclose to the purchaser the facts, extrinsic and intrinsic, which affect the value of the property, constituting the subject matter of the sale?⁶

2) Does the purchaser have such a duty vis-a-vis his vendor?

• I shall also have occasion to examine the concept of a "fiduciary relationship" since this, as has been indicated, bears directly on our problem. Finally, I shall attempt to delineate the true framework in which the decisions are made.

THE VENDOR'S DUTY

The common law was individualistic. A man was entitled to the benefits derivable from his shrewdness. And while, in the business world of the Nineteenth Century, it was not considered proper to overreach, to lie or to use trickery in order to take advantage of a purchaser, one was not required to tell him all that one knew. The courts felt that they were not the protectors of morality, but the dispensers of the rule of law. A classic English case laid down the rule that there is no duty to disclose facts, however morally censurable their non-disclosure may be.⁷

Such was the view of the early cases, and such is essentially still the rule today. The vendor is under no duty to disclose to the purchaser facts which materially affect the value of the property. *Caveat emptor* is the touchstone today as it was in former times. Writers who believe that this caveat has lost much of its content seem to be misreading the bulk of the decisions.⁸ True there are exceptions to and qualifications on the rule. But most of them, upon analysis, seem to resolve themselves into this: an exceptional or peculiar fact pattern may produce a deviating result. But the generality of the general rule suffers little thereby.

*Gayne v. Smith*⁹ involved the sale of land. The vendor was aware of the fact that the water company had the right to condemn the property. The purchaser would not have bought the land had she known this fact, but she made no inquiry. And the vendor was silent. He was silent, that is, toward the purchaser. As to others, he requested them not to mention the facts to the purchaser. *Held*, the vendor was not liable for the concealment. The court felt that the vendor did not actually conceal the fact or divert or forestall an intended inquiry despite the request made

⁶ This article is limited to *such* facts, and does not consider the problem of nondisclosure by the purchaser of his insolvency. This problem is illustrated by the case of *Manly v. Ohio Shoe Co.*, 25 F.2d 384 (4th Cir. 1928).

⁷ *Peek v. Gurney*, L.R. 6 H.L. 377 (1873).

⁸ For example, Comment, 22 BOSTON UNIV. L. REV. 607 (1942)

⁹ 104 Conn. 650, 134 Atl. 62 (1926).

of third parties. Stress was also laid on the fact that the right of condemnation was a matter of record and could be ascertained. At least four qualifications on the rule are enunciated by way of dictum. The first may be expressed in the words of the court.

A vendor of property may not do anything to conceal from the vendee a material fact affecting it or deliberately hide defects, for in so doing he is not merely remaining silent, but is taking active steps to mislead.¹⁰

The court distinguishes between active concealment and mere nondisclosure. This distinction is quite commonly drawn.¹¹ Yet, it is submitted, it is somewhat artificial. There would seem to be a continuum between the two supposed opposites, as there usually is where a sharp dichotomy is set up. Nevertheless, the distinction has some validity, and, if useful, should be applied. Active concealment seems to be morally more reprehensible. Moreover, as shown earlier, active concealment seems to amount to misrepresentation by conduct.

The second qualification is closely related to the first.

the surrounding circumstances may be such that the effect of his [the vendor's] silence is actually to produce a false impression in the mind of the vendee, and [to] lead the vendee to believe that a certain fact exists and so amount to an affirmation of it.¹²

This again refers to misrepresentation by conduct. Here the silence loses its neutrality and, combined with "surrounding circumstances" becomes vocal, if not verbal.

The third qualification is that the vendor may "stand in such a relationship of trust and confidence to the vendee that it is his duty to make a full disclosure." This qualification will be discussed at length later in the article.

The fourth qualification is that if the plaintiff has an opportunity to ascertain the facts he cannot complain of the nondisclosure.¹³

If any of these four situations were present, the general rule would not apply. But, unfortunately for the purchaser, none was found to be present, and he went remediless.

¹⁰ *Id.* at 652, 134 Atl. at 62.

¹¹ "mere silence is quite different from concealment." *Stewart v. Wyoming Cattle Ranch Co.*, 128 U.S. 383 (1888).

¹² *Gayne v. Smith*, 104 Conn. 650, 652, 134 Atl. 62 (1926).

¹³ For example, in *Rothermel v. Phillips*, 292 Pa. 371, 141 Atl. 241 (1928) the plaintiff bought and the defendant sold inventory of a small store. The purchaser had an appraiser make a cursory survey, and, on the strength thereof, he bought at \$7200. He later found much of the stock unsalable. Appraisement revealed that the inventory was worth less than \$500. The plaintiff could not recover because he had had ample opportunity to discover the defects, even though the vendor had previously been afforded better opportunities to become acquainted with the subject matter of the sale.

In sharp contrast to the *Gayne* case is the fairly recent Illinois case of *Forest Preserve District v. Christopher*.¹⁴ Here the defendant leased premises to the plaintiff and failed, though he knew the facts, to reveal that overtures had been made by the Forest Preserve District and that condemnation proceedings might be instituted. The terms of the lease permitted the lessee to improve the premises and erect buildings. Soon after the improvements were completed, condemnation proceedings were commenced. The lessor then sought, in equity, the condemnation award. The lessee sought to have the court reject the application until the lessor "does equity" and purges himself of his bad faith by paying the lessee the reasonable value of the improvements, despite the fact that the real estate was the lessor's and the improvements were fixtures.

The issue was essentially the same as in the *Gayne* case despite the fact that this was not a direct action founded on an alleged fraud. Moreover, the lessor-lessee relationship, particularly where there is involved, an option to purchase, as there apparently was here, is the same, for all practical purposes, as the vendor-purchaser relation.

The lessor argued, as did the vendor in *Gayne*, that the lessor "never asked him for any information regarding the matter."

The court first acknowledged the general rule that in the absence of a duty to speak, silence is not fraud. But then the court spoke of the lessor's "bad faith" and "unconscionable conduct" in dealing with the lessee and declared that "it would be a serious reflection upon equity" if the lessors prevailed in their argument that the facts alleged and proved did not constitute fraud and deceit.

there are times and occasions when it becomes the duty of a person to speak in order that the party he is dealing with may be placed on an equal footing with him.¹⁵

The two cases are clearly contra. The only possible distinction is that in the *Gayne* case the defendant knew that condemnation *might* occur and, in the *Forest Preserve* case, that it would occur. The distinction is too tenuous to be actual. In both cases the defendant knew that it was "in the wind." But in the *Forest Preserve* case, the plaintiff succeeded in pricking the conscience of the court.

In a very recent case, the plaintiff was unsuccessful in doing so, although the defendant knew that certain happenings were "in the wind."¹⁶ Plaintiff contracted to buy a rubbish route from defendant. There were rumors, of which defendant was aware, that the city contemplated letting a contract to pick up combustible rubbish and thus deprive the plaintiff

¹⁴ 321 Ill. App. 91, 52 N.E.2d 313 (1943).

¹⁵ *Id.* at 106, 52 N.E.2d at 319.

¹⁶ *Jappe v. Mandt*, 130 Cal. App.2d 426, 278 P.2d 940 (1955).

of the benefit of his purchase. The court, in holding for the defendant, used the usual clichés; arm's length dealing, no fiduciary relation, full opportunity for plaintiff to investigate the facts. But the real ground for decision appears to be that what defendant failed to disclose were not *facts* and merely *rumors*. Logically, this is unsatisfying. If defendant is under a duty to disclose what he knows, then the fact that what he knows is rumor and not fact should not excuse him. That there is such a rumor in the air is, after all, a fact. The plaintiff should—if the duty exists—be allowed to determine for himself how much credence to place in the rumor. But, despite the lack of logic, the courts seem to be impressed by the criterion of certainty of the "fact" alleged to be concealed, i.e. certainty in the defendant's mind. The instant case distinguished an earlier case in the same jurisdiction,¹⁷ in which the defendant, who was a city councilman, *knew*, by virtue of his position, of official action that had already been decided upon and which would and did have the effect of greatly depreciating the value of the subject matter of the transaction.

Another recent California case is akin to the cases just discussed.¹⁸ This was an action for fraud by purchasers of a resort against the vendors. The alleged fraud consisted in the failure to disclose that part of the improvements were within the right of way of a state highway. The defendant argued *caveat emptor* and pointed to the general rule of "no duty." The court, with little explanation, said "this contention is untenable in the law of fraud" and found that the vendors breached their duty to disclose the information. The court appeared to be blissful in its unawareness of its patently question-begging approach. The very issue was whether this was fraud, and it could not be disposed of by saying, in effect, "you cannot say this is not fraud, because the reasons you urge are not applicable in cases of fraud."

The *Gayne* case is relied on and quoted in a very recent Connecticut decision.¹⁹ The plaintiff here sued to recover the cost of correcting structural defects in a house purchased from the defendant. The latter had mentioned to the plaintiff the depth of the footings for the house and the location of the septic tank, in which two particulars the house did not meet the provisions of the building code. The court, in holding for the defendant, said that the facts presented a case of nondisclosure rather than of deliberate concealment, and stressed that the defendant had not deliberately conceived the purpose of deceiving the plaintiff and of luring him into a false belief. This language indicates that the difference between nondisclosure and concealment may lie in the *intent*, or at least in

¹⁷ *Dyke v. Zaiser*, 80 Cal. App.2d 639, 182 P.2d 344 (1947).

¹⁸ *Kallgren v. Steele*, 131 Cal. App.2d 43, 279 P.2d 1027 (1955).

¹⁹ *Egan v. Hudson Nut Products Inc.*, 142 Conn. 344, 114 A.2d 213 (1955).

the *motive*, of the defendant. Thus delineating the difference does not change the fact that the formula is in reality a semantic device. But if it achieves the goal (so often confronted in the law) of "drawing the line," it is not to be disparaged by calling it "semantic."

The court enunciates the general rule that "mere disclosure does not ordinarily amount to fraud" and qualifies it by stating that it may do so "under exceptional circumstances." Such circumstances are found if there was "a request or an occasion or a circumstance which imposes a duty to speak." But the court does not explain when the duty arises. It does, however, elaborate the hint that intent is material and declares that nondisclosure is actionable for fraud only if the defendant intends or expects to cause a mistake by another, in order to induce him to enter into or refrain from entering into a transaction.

In a strikingly similar case involving nondisclosure of defects as to a septic tank, it was held that the purchaser of a house could not rescind the contract on the ground of fraud even though the sanitary engineer had expressed to the defendant the opinion that the drainage was inadequate, and the latter had not disclosed this to the purchaser.²⁰

The idea that nondisclosure is ordinarily not actionable stems at least in part from the old tort notion that there is a vital distinction between misfeasance or malfeasance, on the one hand, and nonfeasance, on the other. For the latter there was classically no liability unless there was some definite relation between the parties which imposed a duty to speak or act. Thus in *Windram Mfg. Co. v. Boston Blacking Co.*²¹ the plaintiff was in the business of pasting linings to fabrics, using a paste or cement which it purchased from one Ellis. The latter, in turn, purchased it from the defendant-manufacturer who *knew* that it would be used by the plaintiff. The cement was negligently manufactured and mixed and injured the fabrics on which it was used. Defendant knew the facts. The plaintiff sued for negligence and for fraud. As to the fraud the court stated the general rule (and declared it to represent the weight of authority) that there is no liability for bare nondisclosure even though the facts were known, "unless the parties stand in such relation to one another that one is under a legal or equitable obligation to communicate the facts to the other." In an attempt to put flesh on this skeletal principle, the court pointed out that there were no contractual relations between the parties. Apropos, there was no liability for negligence either. The entire argument is reminiscent of the old privity requirement.

Other cases have also cited *Gayne v. Smith*, including one which in

²⁰ *Dozier v. Hawthorne Development Co.*, 37 Tenn. App. 279, 262 S.W.2d 705 (1953).

²¹ 239 Mass. 123, 131 N.E. 454 (1921).

turn has been much cited and quoted.²² Here, plaintiff-purchaser sought to have property impressed with a constructive trust on the theory that it was fraudulent on the part of the defendant-vendor not to disclose that he owned property contiguous to that which he sold to the plaintiff. *Held*, no actionable fraud. By way of dictum the court stated that

Where, before the transaction is completed he [the silent party] knows or suspects that the other is acting under a misapprehension which, if the mistake were mutual, would cause the transaction to be voidable, he is under a duty to disclose the facts.²³

This case apparently came within the rule that a party to a contract to sell land is under no general duty to disclose facts to the other party, rather than the exception just quoted. Many cases are in accord.²⁴

Countless cases deal with the nondisclosure by a vendor of realty of defects in the property itself. The courts seem to be anything but unanimous in their decisions, some adhering to the harsh rule of "no duty," others apparently willing to make an exception in the case of severe defects, especially if they are latent and not readily discoverable even by a diligent purchaser. It is not really possible to reconcile the decisions. A representative sampling of some of the most interesting cases follows.

I will begin with one of the most extreme cases of all.²⁵ The defendant-vendor of a dwelling house knew that the house was infested with termites and that this fact was neither known to nor easily observable by the purchaser. This condition, needless to say, drastically impaired the value of the house, and necessitated substantial expenditures by the plaintiff. Plaintiff alleged all these facts and the further fact that he had exercised due care in inspecting the house. The defendant's demurrer was sustained. The court laid great stress on the fact that the defendant was *silent*. He made no false statements or representations. Nor did he utter a "half truth which may be tantamount to a falsehood." Nor did he prevent the plaintiff from acquiring information as to the condition of the house. The court said that there was nothing to show any fiduciary relation between the parties or confidence and dependence on the part of the plaintiff. "The parties made a business deal at arm's length."

The charge is concealment and nothing more; and it is concealment in the simple sense of mere failure to reveal, with nothing to show any peculiar duty to speak.²⁶

²² Haddad v. Clark, 132 Conn. 229, 43 A.2d 221 (1945).

²³ *Id.* at 233, 43 A.2d at 223.

²⁴ For example, *Salter v. Aviation Salvage Co.*, 129 Miss. 217, 91 So. 340 (1922) in which the vendor concealed from the purchaser the fact that he owned other similar property although he knew that the purchaser was interested in that fact. *Held*, there was no such fraud as would vitiate the contract.

²⁵ *Swinton v. Whitinsville Savings Bank*, 311 Mass. 677, 42 N.E.2d 808 (1942).

²⁶ *Id.* at 678, 42 N.E.2d at 808.

The court refuses to admit, or to realize, that a duty exists *if* the court finds it, that it is not a *condition* to the imposition of liability but a *consequence* thereof.

Many cases rely on the presence of "arm's length" relations. More will be said of this later, but it may be asked at this juncture whether this is not a judicially invented fiction. Are the parties really at arm's length if one is in a superior position to know facts which would, if known to the other, dissuade him from entering into the transaction? And if one does know them, and the other does not; and if the former is aware of the latter's ignorance, and aware, further, that the innocent party could not by reasonable diligence discover the facts; and knowing all this he is silent, are they in any sense at arm's length? It may be wise not to impose liability. But it is not wise to ground the decision on so transparent a fiction as that of an "arm's length" transaction. True, there is no actual duress. There is no verbal deceit. And there is no active hiding of the defect. But is that to say that the parties are at arm's length? Is there not a hidden defect? Is there not, so to speak, a conspiracy between the defendant and the existing circumstances; a conspiracy of silence; a conspiracy to exploit the plaintiff's ignorance? Perhaps this is not so censurable as to justify the imposition of liability, or even the rescission of the contract at the instance of the victim. But the use of fictions, under the circumstances, serves to becloud rather than to clarify the law.

This court finally shows its hand. The decision is *not* based on principle, but on policy. And what is that policy? The court speaks:

If this defendant is liable every seller is liable who fails to disclose any nonapparent defect known to him in the subject of the sale which materially reduces its value and which the buyer fails to discover. Similarly it would seem that every buyer would be liable who fails to disclose any nonapparent virtue known to him in the subject of the purchase which materially enhances its value and of which the seller is ignorant.²⁷

The old familiar bogey: a flood of litigation.

The court also, however, takes a stand on the moral question.

The law has not yet, we believe, reached the point of imposing upon the frailties of human nature a standard so idealistic as this. That the particular case here stated by the plaintiff possesses a certain appeal to the moral sense is scarcely to be denied.²⁸

But the clear implication is that that "appeal to the moral sense" is not so strong as to overcome the considerations of policy. Hence, judgment for the defendant.

²⁷ Swinton v. Whitinsville Savings Bank, 311 Mass. 677, 678, 42 N.E.2d 808 (1942).

²⁸ *Id.* at 678, 679, 42 N.E.2d 808; 809.

*Day v. Frederickson*²⁹ represents an almost equally extreme point of view. Defendant, in selling plaintiff a house, failed to inform him of the defective condition of the plumbing, which was so installed and connected with a cesspool that sewer gas escaped into the house. The court held that the vendor was under no legal obligation to disclose the facts in the absence of a request to do so. Mere silence was not such deceit as would constitute a cause of action for damages.

But, in this area, (nondisclosure of latent defects in realty) most of the cases seem to take the opposite tack and to impose upon the vendor a duty of disclosure, with a correlative liability in the event of a breach. They recognize and enunciate the general rule that the vendor owes no duty of disclosure to the purchaser and then find some exceptional circumstance to justify an exceptional result. Other cases can, however, be found, similar to the two just considered, in which similar or even more unusual circumstances, did not lead to a relaxation of the rule.

Two propositions are commonly stated: (1) If the material facts are accessible to the vendor only, and he knows that they are not known to and are not within the reach of the diligent attention, observation and judgment of the plaintiff, the vendor is bound to disclose them; (2) Where the conditions affect personal health and safety the vendor's duty is greater than where they merely affect the value of the property.

The second of these statements is particularly interesting and is found in quite a few cases. Its interest lies in the fact that the action being prosecuted in no way deals with personal injury such as might have resulted from the defect. It always deals with the complaint that the plaintiff received property of less *value* than he expected.

In *Mincy v. Crisler*³⁰ defendant sold to plaintiff a house situated in part over a covered ditch. The ditch was covered with decayed timber. The defendant was held bound to disclose the facts. The plaintiff, the court declared, had a right to assume that no prudent man would build in that manner. It would seem, although the court did not speak in such terms, that more than mere silence was involved. In the first place, the defendant had *created* the defect, i.e. it was not natural. And, in the second place, the covering of the ditch, although done for purposes of facilitating construction, and not for purposes of concealment, nevertheless amounted to a concealment of the defect. In building in that fashion, the defendant should be held to be representing to all prospective purchasers, though none was then identified or contemplated, that there was no such condition as a ditch. This brings the case into the category of misrepresentation by conduct, even though the conduct was not with ref-

²⁹ 153 Minn. 380, 190 N.W. 788 (1922).

³⁰ 132 Miss. 223, 96 So. 162 (1923).

erence to the particular purchaser. The court emphasized the health and safety factor and the inaccessibility of the facts to the plaintiff.

And in *Weikel v. Sterns*,³¹ where the owner of a lot erected a building with such a sewage pit arrangement as to make the property very uncomfortable on account of the unpleasant odor, an action for damages for fraud was held to lie. This is clearly contrary to the *Day* case discussed above.

There was some evidence that the vendor acted in good faith and without knowledge of the real condition. To this the court replied that "he knew enough facts to put a reasonable man on notice, and when he sold an innocent purchaser the house, causing him a loss by reason of the concealment of the facts, the loss should fall on him and not on the purchaser."³²

In *Kaze v. Compton*,³³ the purchasers of a house sued in deceit for the vendor's alleged concealment of the existence of a drain tile which ran beneath the house and caused water to accumulate under the house and in the yard. After a verdict for the plaintiff the trial court sustained the vendor's motion for summary judgment. On appeal it was reversed on the ground that under the state of the evidence summary judgment was improper. The court also discussed the substantive issue in the following terms.

If deception is accomplished, the form of the deceit is immaterial. And the legal question is not affected by the absence of an intent to deceive, for the element of intent, whether good or bad, is only important as it may affect the moral character of the representation.³⁴

The court cited the *Weikel* case and pointed out that in the case at bar the concealed condition was not so extreme as in that case. There it was inherently damaging, while here it was potentially so. "But the condition was substantial or vital enough to place a duty upon the vendors to disclose it."³⁵ In other words, the *severity* of the *defect* is an important criterion of the duty of disclosure. If it is severe enough, then mere negligence on the part of the defendant in not learning of it may be a sufficient predicate of liability. If it is less substantial, his motive and intent become material.

In another case the defendant owned two residential lots. He knew that they had been filled with debris in 1928 and had been covered so that the fact of the filling did not appear from a casual examination of

³¹ 142 Ky. 513, 134 S.W. 908 (1911).

³² *Id.* at 514, 134 S.W. at 909.

³³ 283 S.W.2d 204 (Ky. 1955).

³⁴ *Id.* at 207.

³⁵ *Kaze v. Compton*, 283 S.W.2d 204, 208 (Ky. 1955).

the property. The fact of filling materially increased the cost of building. In 1940, the defendant sold the lots to the plaintiff. The latter saw the lots and made no inquiry as to whether they were filled or not, and the defendant made no verbal representations. After discovering the fact, the plaintiff sought to rescind the transaction. In a very short opinion the court held for the plaintiff. The points emphasized were the vendor's knowledge, the purchaser's ignorance and the inaccessibility of the facts.³⁶

*Rothstein v. Janss Investment Corp.*³⁷ involved almost identical facts. Here the court allowed the purchaser to recover damages for fraud and deceit. The damages resulted from the fact that the fill necessitated the use of deep and expensive foundations. The purchaser had inspected the premises, but in view of the latent nature of the defect, this was not a defense.

A Washington court articulated the principle under consideration by saying that a lessor must disclose *concealed* defects which are known to him and not easily discoverable.³⁸ The court declared that normally there is no implied covenant by a landlord that the demised premises are fit for the purposes for which demised. Yet here, where the lessor failed to disclose that the basement of a building leased for an automobile agency was subject to flooding during the rainy season and that, as a result, the heating plant was rendered useless, the fraud barred the lessor from recovering rent after the lessee had left the premises.

Finally, *Greenberg v. Glickman*³⁹ allowed the plaintiff-purchaser of realty to recover for fraud against the vendor when the defendant failed to disclose a sub-surface water condition which resulted in the flooding of the basement of a residence building constructed by the defendant. The court admitted that "the relationship of the parties was unaffected by any fiduciary obligation" and that by the general rule "the seller was under no duty to disclose to the plaintiff all of the circumstances affecting the value of the subject matter of the sale."⁴⁰ But, the court said, "there may be circumstances, where the failure to disclose facts known to the seller and unknown to the buyer may be tantamount to concealment."⁴¹ Such circumstances were here found to exist. The reason seems to be that since the defendant contracted to erect a building with a finished base-

³⁶ *Clauser v. Taylor*, 44 Cal. App.2d 453, 112 P.2d 661 (1941).

³⁷ 45 Cal. App.2d 64, 113 P.2d 465 (1941).

³⁸ *Perkins v. Marsh*, 179 Wash. 362, 37 P.2d 689 (1934).

³⁹ 50 N.Y.S.2d 489 (1944) *modified*, 268 App. Div. 882, 51 N.Y.S.2d 96 (1945), *appeal denied*, 268 App. Div. 987, 51 N.Y.S.2d 861 (1945).

⁴⁰ *Greenberg v. Glickman*, 50 N.Y.S.2d 489, 491 (1944).

⁴¹ *Id.* at 491.

ment, it "invited the impression that there were no conditions below the surface of the land that would affect the utilization of the basement."⁴²

Thus we see that in the case of a vendor of realty most courts are inclined to impose on him a rather strict duty of disclosure of *latent* defects in the property. On one theory or another they make an exception to the usual rule. The most emphasized point is the difficulty or impossibility of the purchaser's discovering the defect for himself. That is to say, the duty of discovery is not cast upon the purchaser although he could, presumably, learn of the defect if he paid for a thorough, expert investigation. This appears to be sound, for if the defect were discovered and the contract of purchase not consummated, (because the vendor would not agree to a satisfactory downward adjustment in the purchase price) the purchaser is out-of-pocket to the extent of the cost of the investigation. The more serious the defect, the more hidden, and the more dangerous to personal health — the more likely are the courts to find nondisclosure tantamount to fraud. At a certain point, the vendor will be held responsible even if he was, in fact, ignorant of the defect.

Some courts impose liability on the vendor, or at least allow rescission by the purchaser, where the undisclosed fact was not a latent defect in the property but a "defect" in the *amount* of property being conveyed. So, where the purchaser, known to the defendant-vendor, believed that a driveway and a garage were on the latter's property, the plaintiff was permitted to rescind.⁴³ On the other hand, it has been held that the mere failure of a vendor of realty to refer the vendee to his record muniments of title or the judicial decisions bearing upon it, is not such fraud as to deprive him of the benefit of the rule that damages will not be awarded against a good faith vendor who is unable to convey a good title.⁴⁴

Several cases have been found in which the vendor of realty failed to disclose to the purchaser the fact that the vendor had been making an unlawful use of the property. From the point of view of the purchaser's loss traceable to the undisclosed fact, there is no difference between non-

⁴² The court added, "With knowledge of the existence of subsurface water and the likelihood of its seepage through the basement floor, the silence of the defendant amounted to the suppression of a highly material fact."

⁴³ *O'Shea v. Morris*, 112 Neb. 102, 198 N.W. 866 (1924).

⁴⁴ *Crenshaw v. Williams*, 191 Ky. 559, 231 S.W. 45 (1921). See also *Jewell v. Allen*, 188 Okla. 374, 109 P.2d 235 (1941). This was a damage action for deceit. Plaintiff bought from defendant an undivided royalty interest in the oil rights covered by an oil and gas lease. Both of the parties were lease brokers. Defendant failed to inform plaintiff that the lease referred to additional acreage and contained a provision giving the owner of the royalty in the additional acreage a right to share in the well produced on the land from which plaintiff received his royalty. *Held*, the failure to so inform did not constitute fraud. The court emphasized plaintiff's experience as a lease broker and his presumed familiarity with such transactions.

disclosure of such a fact and of any other. It is certainly of no greater materiality. Yet the cases seem uniformly to allow a recovery or rescission as the case may be, by the misled purchaser. One almost feels from reading these cases that the courts are penalizing the vendor not so much for his failure to make full disclosure, as for the unlawful manner in which he operated his own property.

For example, in *Burzillo v. Thompson*⁴⁵ the defendant-vendor of an apartment building stated that the rent for a particular apartment was \$150 a month furnished, and failed to disclose that the ceiling rental was \$60 a month unfurnished and that his application to the Rent Administrator for a ceiling rental of \$150 a month was pending. Actually, the vendor was collecting a rental of \$150 a month in violation of the then applicable law. The court held that the purchaser was entitled to rescind the contract and recover his deposit money.

In another case,⁴⁶ the same court went into more detail in its opinion. Here there was a representation by the vendor⁴⁷ of a roominghouse that the rentals were \$297 a month. And so they were. But they were in excess of the ceiling rental. The trial court held that the plaintiff did not make out a prima facie case. The appellate court reversed and held that the purchaser had a cause of action in fraud for damages. The court said that the plaintiff was entitled to believe that the rentals being collected were lawful (Query).

Defendant had no right to withhold from plaintiffs the highly material and important information that the \$297 rental had not been lawfully approved. Though he was telling the literal truth, he was really telling only a half-truth.⁴⁸

The court then analogized the situation to one where the vendor reveals some defect in the property and conceals or remains silent as to other defects, latent in their nature, and concluded "there can be no doubt that in this case there was misrepresentation by suppression."

The reader may well inquire why the plaintiff is not barred by his failure to ascertain the facts. Surely they were a matter of public record. The court rejected this argument, saying that the plaintiffs rightfully relied on the defendant's statement and were justified in assuming that their vendor had not violated the Rent Act. "In these circumstances, the rule of *caveat emptor* does not apply."⁴⁹ The court gives no reason in support of this statement, but merely cites and quotes a case⁵⁰ in which there

⁴⁵ 57 A.2d 195 (Mun. Ct. App. D.C. 1948).

⁴⁶ *Tucker v. Beazley*, 57 A.2d 191 (Mun. Ct. App. D.C. 1948).

⁴⁷ The case actually involved a lease with option to purchase.

⁴⁸ *Id.* at 193.

⁴⁹ *Tucker v. Beazley*, 57 A.2d 191, 194 (Mun. Ct. App. D.C. 1948).

⁵⁰ *Lester v. Superior Motor Car Inc.*, 117 F.2d 780 (D.C. Cir. 1941).

was (1) an actual misrepresentation and (2) information peculiarly in the vendor's knowledge.

There was, as might be anticipated, a vigorous dissent. Among other things the dissent argues that the plaintiff had more duty to *inquire* about rent ceilings than the defendant to speak.

While the doctrine of caveat emptor may be less rigorously enforced today than formerly the law still requires a purchaser to use reasonable care for his own protection.⁵¹

Both of these rent ceiling cases might be explained by the fact that there was more than silence, i.e. there was a representation which, while literally true, conveyed, under the circumstances, a false impression. But it is believed that a more likely explanation is that already suggested, viz. the desire to penalize a reprehensible defendant.

This motive is even more clearly illustrated in the interesting case of *Ikedda v. Curtis*.⁵² Here, plaintiffs bought a hotel from defendant. Defendant stated that there was a certain amount of income and that it came from permanent and transient guests. The income was even greater than represented, and the source was as stated. But, to the plaintiff's embarrassment and chagrin, the principal source of income was from the use of the premises for purposes of prostitution. The court held that the plaintiffs felt, and "naturally" so "that they were buying a legitimate business." Plaintiffs recovered damages for the fraud. No explanation is discernible for the imposition of the duty other than the nature of the vendor's occupation.

In another case, a contract for the sale of land was held unenforceable for reasons of public policy because the vendor did not disclose that his profit was inordinate and unfair.⁵³

But not all the instances of undisclosed illegality produce the same result. In *Watt v. Patterson*⁵⁴ the defendant sold her roominghouse to the plaintiff. Actually the property was in a single-residence zone. The court held that the mere fact that defendant had been operating a roominghouse did not constitute an actionable misrepresentation that the house was legally available as such. The key point was that the defendant was unaware of the restriction. The reasoning suggested above seems to apply. Here the defendant's conduct was — because of his ignorance — less censurable. The court also discussed the fact that at most the representation was one of an opinion or one of law.

⁵¹ See note 49 *supra*.

⁵² 43 Wash.2d 449, 261 P.2d 684 (1953).

⁵³ *Hagge v. Drew*, 157 P.2d 408 (Cal. App. 1945). The land was to be used to build homes for war workers, and the transaction was under the Federal Housing Act.

⁵⁴ 125 Cal. App.2d 788, 271 P.2d 200 (1954).

In cases of the sale of chattels the problem of nondisclosure may be intimately bound up with the problem of warranty. Frequently the law implies certain warranties, and a failure to disclose the existence or non-existence of a fact, may create a dual cause of action: (1) breach of warranty and (2) misrepresentation. So far as can be determined, no particular practical significance attaches to this dualism.

The cases indicate, for example, that the buyer of an automobile from a dealer or manufacturer may, in the absence of an understanding or knowledge to the contrary, assume that it is new.⁵⁵ In an early case,⁵⁶ the defendant-dealer sold and the plaintiff bought a mowing machine under a written contract containing an express warranty that the machine was "good and well made" and would "do as good work as any other machine in its class." The terms of the warranty were literally complied with, but the machine was second-hand. The purchaser was allowed to recover. Newness of the machine was implied. Strictly speaking, the case was not decided on a theory of misrepresentation. But, analysis indicates that it is the silence of the vendor which was held blameworthy.

In *Donovan v. Aeolian Co.*⁵⁷ the plaintiff purchased a piano, believing it to be new. It was, in fact, used and reconditioned. In New York, at least as of the date of that case, there was no warranty of newness implied in law. And the court stated broadly that if the seller does not know that the buyer is acting under the belief that the article is new and has done nothing to induce the belief, the buyer cannot complain. Silence is not actionable so long as it is "consistent with honest dealing" and "does not constitute deception." Here, the plaintiff recovered, the jury having found that defendant's salesman knew that the plaintiff thought the piano was new.

Statutes in some jurisdictions provide that an implied warranty or condition as to quality or fitness for a particular purpose may be annexed by the usage of the trade.⁵⁸

Other cases, with or without the application of statutes, reach similar results in the case of the sale of animals and of meat.⁵⁹

⁵⁵ *Stewart v. Potter*, 44 N.M. 460, 104 P.2d 736 (1940).

⁵⁶ *Grieb v. Cole*, 60 Mich. 397, 27 N.W. 579 (1886).

⁵⁷ 270 N.Y. 267, 200 N.E. 815 (1936).

⁵⁸ Under such a statute, *Fox v. Boldt*, 172 Wis. 333, 179 N.W. 1 (1920) held that where defendant purchased a tractor from plaintiff, there was an implied warranty that the machine delivered would be new. Therefore, on delivery of a secondhand machine, the defendant was entitled to offset his damages from the breach of such warranty against the balance due on the purchase price. The court took judicial notice of the trade usage which comported with the assumption of newness.

⁵⁹ *Rinaldi v. Mohican Co.*, 225 N.Y. 70, 121 N.E. 471 (1918) (NEW YORK PERSONAL PROPERTY LAW, §96, as added by Laws 1911, c. 571). But see *Barton v. Dowis*, 315 Mo. 226, 230, 285 S.W. 988, 989 (1926). The latter declares: "In the

There remains to be considered one group of cases, those dealing with the sale of corporate securities.

*Lovell v. Smith*⁶⁰ was an action by a subscriber for the stock of a corporation of which the defendants were the promoters and directors. The defendants had not disclosed, in the prospectus used in soliciting stock subscriptions, that they had secured their stock on more advantageous terms than those on which it was being offered to the public and to the plaintiffs, and that they (the defendants) had procured, at the outset, voting control over the company. Had these facts been disclosed, plaintiff would not have subscribed for the stock. The trial court found that no statements in the prospectus were fraudulent or calculated to deceive the plaintiff. On appeal, the judgment for the defendant was affirmed. The court held that no duty of disclosure existed, because no fiduciary relation existed.

On the other hand, in *Stern v. National City Co.*⁶¹ the plaintiff, who purchased securities from the defendant, successfully maintained that the sale impliedly represented that the securities were properly registered under the applicable Blue Sky Laws.⁶² The court said:

The rule of caveat emptor has been modified, and the sale itself may give rise to implied representation just as effectively as though the seller had made express statements to the same effect.⁶³

The distinction between these two cases would seem to lie in the nature of the undisclosed fact. In the latter it was one which the sale implied; in the former it is doubtful whether that is so. But, the true difference, it is submitted, is in the attitude toward the relation subsisting between plaintiff and defendant. If the relation were fiduciary, both facts would be reasonably implied, if it were not, neither would. More will be said later about the nature of a fiduciary relation.⁶⁴

sale of animals, the rule of caveat emptor applies and there is no implied warranty that the animals are free from disease. That, of course, applies where the seller is ignorant of any disease with which the animal may be affected and where both the seller and the buyer are equally informed and have equal opportunities for inspection of the animal. If the seller knows, or has reason to know, the animal he sells is afflicted with a disease not known to the purchaser and not discernible on inspection, he is guilty of fraud." The quoted statement is, however, dictum since it was found that the seller was innocent, and a judgment for the plaintiff-buyer was reversed.

⁶⁰ 232 Ala. 626, 169 So. 280 (1936).

⁶¹ 25 F. Supp. 948 (D. Minn. 1938), *aff'd*, 110 F.2d 601 (8th Cir. 1940), *rev'd on a procedural point*, 312 U.S. 666 (1940).

⁶² The statute of limitations was involved, and, in order to avoid being barred thereby, plaintiff had to show that his action sounded in fraud.

⁶³ *Stern v. National City Co.*, 25 F. Supp. 948, 956 (D. Minn. 1938).

⁶⁴ See *Playland Park Stadium Corp. v. J. H. Spector and Sons*, 253 S.W.2d 466 (Tex. Civ. App. 1952). This was an action against a corporation and individuals for

SUMMARY OF THE GENERAL RULE AND ITS EXCEPTIONS

Aside from the broad exception for misrepresentation by conduct, certain other fact patterns deviate from the general rule of "no duty." These apply as well to the purchaser's liability as to the vendor's, but it seems convenient to outline them at this point.

If there is, in addition to silence, any statement which tends *affirmatively* to a suppression of the truth, or to the withdrawal or distraction of the other party's attention from the real facts, the concealment becomes fraudulent.⁶⁵

If the purchaser makes inquiries, and the vendor answers evasively, and in such a manner as to mislead, he is liable even though there was no affirmative misrepresentation.⁶⁶

Suppose the vendor has previously made a true statement as to the condition of the property, and, before the transaction is consummated, the conditions change. Although there are some cases to the contrary, the better view would seem to be that under such circumstances, the vendor has a duty to disclose the change.⁶⁷ Sometimes the court attempts to analyze the earlier statement and to determine whether it was a continuing representation or one which related only to the then existing state of affairs.⁶⁸ If it was the latter, there is no liability for the subsequent silence. The distinction seems tenuous.

One of the principal exceptions remains to be commented upon. While silence alone may not be actionable, if the vendor undertakes to speak, he must not conceal anything which would tend to qualify or contradict the facts which he had stated. In other words, to tell half of the truth is to make a half-false representation. For example, *Coral Gables, Inc. v. Mayer*⁶⁹ was an action on some promissory notes brought by the successor to the payee corporation against the maker. The notes had been given in payment for property bought by the maker from the payee. The defendant counterclaimed on, among other grounds, the ground of fraud in the sale of the property. The corporation's agent had described the attractive features of the property's location and told the truth, as far

rescission and for damages incurred in the purchase of debentures issued by the defendant corporation. The defendants failed to disclose the exact nature of the ownership of property which affected the security for the notes. The court, without discussion, found a duty of disclosure and held the defendant liable for fraud.

⁶⁵ *Ash Grove Lime & Portland Cement Co. v. White*, 361 Mo. 1111, 238 S.W.2d 368 (1951).

⁶⁶ *Southern v. Floyd*, 89 Ga. App. 602, 80 S.E.2d 490 (1954).

⁶⁷ *Childress v. Nordman*, 238 N.C. 708, 78 S.E.2d 757 (1953).

⁶⁸ *Ibid.*

⁶⁹ 241 App. Div. 340, 271 N.Y. Supp. 662 (1934), *aff'd*, 246 App. Div. 518, 282 N.Y. Supp. 596 (1935), *aff'd*, 270 N.Y. 670, 1 N.E.2d 991 (1936).

as he went. But he omitted to advise the purchaser of the proximity of "obnoxious business developments" which would have an adverse effect on real estate values. The trial court excluded the issue of fraud from the jury's consideration. Judgment for the plaintiff (the vendor's successor) was reversed, and the courts held that it was a question for the jury whether nondisclosure of these facts amounted to fraud. The jury should have been charged as follows:

Every word you say may be true; but if you leave out something which absolutely qualified it, you may make it a false statement.⁷⁰

This proposition is both sensible and salutary. But if too broadly or literally applied it would destroy the rule which relieves the vendor of the duty of disclosure. The courts speak of "mere silence." Yet a business transaction is never entirely without conversation, and verbal exchanges nearly always involve, expressly or by implication, representations of fact. The vendor may be silent as to some features or topics, while he is articulate as to others. Does this deprive him of the privilege of nondisclosure? This would clearly result if the "half-truth" principle were loosely applied. But it is not so applied. In fact, it is reserved for those cases in which so much is said that there is an implied representation that there is no qualifying fact which remains unreported. That is to say, liability will be imposed where the undisclosed fact would place an *absolute* qualification on the disclosed facts. It is almost a case of misrepresentation by conduct, the conduct consisting of the act of saying so much that it implies that nothing material remained unsaid. An analogy may be drawn to the general principle of tort law that where a defendant has no duty to act, if he undertakes or assumes to act, and should foresee risks to the plaintiff, he must carry out his undertaking with reasonable care.

Pomeroy has stated the general rule as follows:

Ordinarily, no duty of disclosure exists except (1) where there is a previous confidential relation between the parties; (2) where it appears one or each of the parties expressly reposes a trust or confidence in the other; (3) or where the contract or transaction is intrinsically fiduciary and calls for good faith, as in cases of insurance contracts the rule of caveat emptor generally applies to sales of land.

In ordinary contracts of sales, where no previous fiduciary relation exists, and where no confidence express or implied growing out of or connected with the very transaction itself, is reposed on vendor, and the parties are dealing with each other at arm's length, and the purchaser is presumed to have as many reasonable opportunities for ascertaining all the facts as any other person in his place would have had, then the general doctrine already stated applies; no duty to disclose is not a fraudulent concealment.⁷¹

This is assuredly the rule as it affects silence on the part of vendors.

⁷⁰ *Id.* at 342, 271 N.Y. Supp. at 664.

⁷¹ 3 POMEROY, EQUITY JURISPRUDENCE § 904 (5th ed. 1941).

Yet, as we have seen, the courts, in a wide variety of situations, reach results which are not consistent with the rule. This is not to deny the authority of Pomeroy or to deny the validity of the rule. It is only to point up the famous maxim that general rules do not solve particular cases. In short, one might say that the vendor hardly ever has a duty to disclose facts affecting the value of his property. But there are numerous exceptions in addition to those which Pomeroy has indicated.

THE PURCHASER'S DUTY

In summarizing (admittedly in an over-simplified manner) the duty of the vendor to disclose material facts to his purchaser, I concluded that he "hardly ever" is under such a duty. When we turn to the other side of the vendor-purchaser relation and inquire as to the duty of the purchaser to make such disclosures we find he is "almost never" under an obligation to do so. The distinction between "hardly ever" and "almost never" is a real one. Only in relatively few circumstances does the law impose a duty of disclosure on the purchaser. Pomeroy, in discussing the vendor's duty, declares that

it has never been contended, in our system of jurisprudence, that a vendor in a contract of sale is bound to disclose all facts which, if known by the buyer, would prevent or tend to prevent him from making the purchase.⁷²

But when he comes to the subject of present inquiry he says

Much less has it ever been maintained that the buyer is bound to discover all facts known to himself which would enhance the value of the article sold or affect the conduct of the vendor.⁷³ (emphasis supplied)

The general rule is stated quite directly in *James v. Anderson*.⁷⁴

One who is a prospective land buyer owes no duty in his dealings with the owner to disclose any possible events or present or future conditions that may greatly enhance the value of the land.⁷⁵

In *Grenlac Holding Corp. v. Kahn*⁷⁶ the plaintiff-purchaser of realty sought specific performance of the contract. The vendor counterclaimed for fraud and deceit alleging that the purchaser had knowledge of the pendency of rezoning proceedings which would make the realty more valuable. *Held*, summary judgment for plaintiff; he owed no duty to his vendor to disclose his motive in purchasing the property. The court ad-

⁷² POMEROY, *op. cit. supra* note 71, at § 901.

⁷³ *Ibid.*

⁷⁴ 149 Va. 113, 140 S.E. 264 (1927)

⁷⁵ *Id.* at 122, 140 S.E. at 264.

⁷⁶ 106 N.Y.S.2d 83 (1951).

ded the usual statement that there was no fiduciary relationship and that the parties were dealing at arm's length.

The point was also made that the pendency of the rezoning application was a matter of public record and ascertainable by the vendor on investigation. There is a veiled implication that had the facts been peculiarly in the purchaser's possession the result might have been different. Such implications are the weakest and least reliable of dicta. The court ridiculed the vendor's "lack of diligence" and praised the purchaser's "business sagacity." The latter was justified in using that ability for his "monetary advantage."

The cases thus far introduced have not discussed the logic or policy of the rule. Two much earlier cases, one English and one American, do so. *Fox v. Mackreth*⁷⁷ poses a hypothetical case in which the purchaser knew of some secret intrinsic value of the vendor's property such as, for example, a mine. The vendor is ignorant of the facts, and the purchase price does not take them into consideration. The purchaser does not disclose the facts. The English court said that under the circumstances, a court of equity cannot set aside the bargain. The reason given is not that the one party is unaware of the unreasonable advantage taken by the other of his knowledge, but that there is no contract between them which requires such a disclosure.

if it were otherwise, such a principle must extend to every case in which the buyer of an estate happened to have a clearer discernment of its real value than the seller. It is therefore, not only necessary that great advantage should be taken in such a contract and that such an advantage should arise from a superiority of skill or information, but it is also necessary to show some obligation binding the party to make such a disclosure.⁷⁸

*Trigg v. Read*⁷⁹ contains a similar discussion. Again it is contended that the purchaser need not disclose the facts. The vendor "is supposed to know the value and qualities of his own property."⁸⁰ The purchaser may reap the profit of his superior skill or diligence. The cases supporting this proposition are legion.

Some cases seem to be aware of the ethical question involved, but they dispose of it quickly. In one case, for example, it was alleged that the agent of the purchaser withheld from the grantor information to the effect that the property was rapidly increasing in value by reason of im-

⁷⁷ 2 Cox, Ch. 320, 30 Eng. Rep. 148 (1788).

⁷⁸ *Id.* at 321, 30 Eng. Rep. at 149.

⁷⁹ 24 Tenn. 529, 42 Am. Dec. 447 (1845).

⁸⁰ See Annot. 56 A.L.R. 429 et seq. (1928). The annotator states that "if the vendor is so indiscreet as to place reliance upon the statement of a prospective purchaser, without finding out the truth for himself, he should be left to make the best of a bad bargain."

provements in a nearby city. The court asserted that "whatever moral or ethical duty there may have rested on [the purchaser] to furnish complainant [vendor] such information" there was no legal obligation.⁸¹

Hays v. Meyers,⁸² goes still further in its emphasis on the right of a purchaser not to disclose the knowledge he has acquired. Not only is no legal duty found to exist, but the non-disclosure is condoned, possibly praised, on moral grounds.

A person may with *perfect honesty and propriety* use for his own advantage the superior knowledge of property he desires to purchase, that has been acquired by skill, energy, vigilance and other legitimate means [and is under no obligation to disclose it.]⁸³ (emphasis supplied)

The same court formulates the most impressive policy argument found in the cases to justify the rule.

If any other rule were adopted, it would have a depressing tendency on trade and commerce by removing the incentive to speculation and profit that lies at the foundation of almost every business venture.⁸⁴

A radical change in the law in this area *would* work havoc to the profit system.

In *Holly Hill Lumber Co. v. McCoy*⁸⁵ the purchaser sought specific performance of a land contract. The vendor's defense was the fraudulent failure of the purchaser to reveal the existence of a valuable lime deposit on the land. In an extremely well-reasoned opinion, the court enunciates the general doctrine, quotes Pomeroy, analyzes the circumstances in which a duty of disclosure will be found to exist and seeks to apply these broad principles to the vendor-purchaser relation. But the cogency of the generalized reasoning is dissipated by the final statement; "Of course, each case must depend upon its own circumstances."⁸⁶ In the instant case the presidents of both plaintiff and defendant corporations were "business men of experience and capacity" and had had previous dealings with each other. These circumstances were sufficient, or so concluded the court, to make the transaction one at arm's length. Hence, there was no duty of disclosure. As a post script the court added that the evidence showed no "guilty knowledge," or "bad faith" on the part of the purchaser, as if to imply that motive or intent might be a factor of decisive weight. And so it might, in a proper case.

⁸¹ *Pratt Land & Improvement Co. v. McClain*, 135 Ala. 452, 33 So. 185 (1902). See also *Terrell v. Marion County*, 250 Ala. 235, 34 So.2d 160 (1948).

⁸² 139 Ky. 440, 107 S.W. 287 (1908).

⁸³ *Id.* at 442, 443, 107 S.W. at 288.

⁸⁴ *Hays v. Meyers*, 139 Ky. 440, 443, 107 S.W. 287, 288 (1908).

⁸⁵ 201 S.C. 427, 23 S.E.2d 372 (1942)

⁸⁶ *Id.* at 438, 23 S.E.2d at 377

Some cases reach the same result even where the purchaser actively represented that the land had less value than it actually had. Such was the case, for example, when the purchaser represented that certain realty was valuable only for timber and, in fact, it contained iron, a fact known to both parties, but the true value of which was known only to the purchaser.⁸⁷

In discussing the vendor's duty of disclosure, I pointed out that while silence alone might not be actionable, any conduct or circumstances which adds significance to the silence might be a sufficient basis on which to ground a cause of action. The same is true in the case of the purchaser.

Not only a single word but "a nod or a wink or a shake of the head, or a smile from the purchaser might defeat the application of the principle that mere reticence on the part of the purchaser does not in law amount to fraud."⁸⁸

Moreover, mere silence will be enough if the court is willing to "find" a duty of disclosure. Before it will do so, it will require a fiduciary or quasi-fiduciary relation. The nature of this relation will be discussed in the next section.

There are some cases, though they represent a minority, which impose liability on the purchaser for a mere nondisclosure, without requiring, as a predicate, the existence of a fiduciary relation. Most of these cases involve unusual circumstances of such a nature that to hold otherwise would work an egregious injustice. Yet, it cannot be denied that they are, in tenor at least, asserting a different attitude toward the underlying substantive problem.

Perhaps the leading American case which gives a measure of recognition to the existence of a duty is *Laudlaw v. Organ*,⁸⁹ decided by the United States Supreme Court in 1816. The purchaser, under a contract for the sale of tobacco, having advance information of the Treaty of Ghent which enhanced the value of the facts, repossessed the tobacco. In this action, the buyer sought to retake it and to get damages. The issue was whether the purchaser was under a duty to communicate to the vendor "the intelligence of extrinsic circumstances which might influence the price" and which was exclusively in his knowledge. The Supreme Court held that he was not bound to communicate it *but* reversed a judgment for the plaintiff-purchaser because the verdict had been directed. The question whether any imposition had been practiced by the purchaser was properly for the jury. The court would not, at that time, decide the question as a matter of law.

⁸⁷ *Williams v. Spurr*, 24 Mich. 335 (1872).

⁸⁸ *Chandler v. Butler*, 284 S.W.2d 388 (Tex. Civ. App. 1955)

⁸⁹ 15 U.S. (2 Wheat.) 178 (1817).

The most interesting aspect of the reported case is the argument of opposing counsel. It will be useful to quote the central section of each. Counsel for the plaintiff-purchaser argued:

on principle, he was not bound to disclose. Even admitting that his conduct was unlawful, in *foro conscientiae* does not prove that it was so in the civil forum. Human laws are imperfect in this respect, and the sphere of mortality is more extensive than the limits of civil jurisdiction. The maxim of caveat emptor could never have crept into the law if the province of ethics had been co-extensive with it. There was, in the present case, no circumstance or manoeuvre practiced by the vendee, unless rising earlier in the morning and obtaining by superior diligence and alertness that intelligence by which the price of commodities was regulated, be such. It is a romantic equality that is contended for on the other side. People never can be precisely equal in knowledge, either of facts or of the inferences from such facts, and both must concur in order to satisfy the rule contended for. The absence of all authority in England and the United States — both great commercial countries — speaks volumes against the reasonableness and practicality of such a rule.⁹⁰

To this, counsel for the defendant-vendor replied:

Though the record may not show that anything tending to mislead by positive assertion was said by the vendee yet it is a case of manoeuvre, of mental reservation, of circumvention. The information was monopolized by the messengers from the British Fleet, and not imparted to the public at large until it was too late for the vendor to save himself. The rule of law and of ethics is the same. It is not a romantic, but a practical and legal rule of equality and good faith that is proposed to be applied.⁹¹

These arguments project what is, at least for this writer, the nub of the problem: What should be the generative or causal relation between the dictates of ethics and the rule of law? I shall return to this question and attempt to define it more precisely in the last part of this article.

*Delorac v. Conna*⁹² illustrates the type of situation in which courts might be inclined to impose a duty. The owner of Nebraska land resided in California. He was not in a position to know his own land, and he therefore had a right to rely on the purchaser's honesty. The decision is weakened by the fact that the purchaser was not silent, but made positive and false statements as to the value of the land. In another case the vendor of a farm, who had never seen it, could secure its reconveyance where the purchaser concealed his knowledge that it contained a granite quarry.⁹³

⁹⁰ *Id.* at 193, 194.

⁹¹ *Lardlaw v. Organ*, 15 U.S. (2 Wheat.) 178, 194 (1817).

⁹² 29 Neb. 791, 46 N.W. 255 (1890).

⁹³ *Crompton v. Beedle*, 83 Vt. 287, 75 Atl. 331 (1910). *Stackpole v. Hancock*, 40 Fla. 362, 378, 24 So. 914, 918 (1898) after stating the general rule, asserts that if the purchaser "undertakes [to disclose facts or answer inquiries] he must disclose the whole truth, without concealment of material facts, and without doing anything calculated to prevent an investigation on the part of the vendor, especially if he does

More interesting is a case⁹⁴ in which the plaintiff-purchaser sued for the delivery of rice under a contract, the rice having been sold by description and sample. The vendor's agent had made an error and was selling a high-grade, expensive rice for a cheaper one. The court held that as long as the plaintiff was unaware of the error, he was entitled to the rice, for, the parties dealt on an equal footing, neither knowing the facts. But as soon as the plaintiff learned of the error, he could neither recover damages under the contract nor insist on delivery, "for, having knowledge of the mistake under which the defendant was laboring, it would be a fraud on his part to take advantage of it."⁹⁵ The case is an example of a rare species. The more orthodox dissent argued that the plaintiff had acted honorably and was entitled to the benefit of his contract. Other cases in point are discussed in the notes.⁹⁶

Thus, it is seen, only in rare situations does the law cast upon a purchaser the duty to impart his special knowledge to his vendor. He is generally not penalized for his nondisclosure, and, on the contrary, is permitted to derive a benefit from his shrewdness, his perception and his diligence.

not reside near the land, and the vendee does." (emphasis supplied) And the court added that "a very little is sufficient to effect the application of this principle, and statements ordinarily regarded as an expression of an opinion may be considered as sufficient when calculated to mislead and prevent an examination of the property on the part of the vendor."

⁹⁴ *Davis v. Reisinger*, 120 App. Div. 766, 105 N.Y. Supp. 603 (1907)

⁹⁵ *Id.* at 768, 105 N.Y. Supp. at 604.

⁹⁶ In *Conlan v. Sullivan*, 110 Cal. 624, 42 Pac. 1081 (1895) the purchaser knew, but failed to communicate the fact, that his vendor was laboring under a mistake as to the existence of a mortgage on the property. *Held*, the vendor could rescind the sale, where the purchaser's intent was to defraud the vendor out of the amount of the supposed mortgage.

In *Noved Realty Co. v. A. A. P. Co.*, 250 App. Div. 1, 293 N.Y. Supp. 336 (1937) the defendant corporation obtained a \$3000 deduction in the price for which it purchased a second mortgage by representing that the existence of a record and unpaid conditional sales contract covering property on the premises would require the expenditure of at least \$3000. The defendant did not disclose that the conditional sales contract had been secured by the deposit in escrow of \$5500 (its face) in a transaction in which the defendant had bought participation in the first mortgage. Said the court: "there are limits beyond which parties in that relation (vendor-purchaser) may not go in the concealment of material facts. We think that limit was reached and passed." *Held*, the corporation is liable to the seller of the second mortgage.

And where a representative of the purchaser of standing timber obtained a third party to conduct a cruise of the timber both for himself and for the vendor, to determine the amount of timber on the vendor's land, the purchaser's representative was held to be acting not only for himself but as agent of the vendor and therefore owed the latter a positive duty of full disclosure regarding the results of the cruise. *Dahl v. Crain*, 193 Ore. 207, 237 P.2d 939 (1951).

THE PROBLEM OF THE FIDUCIARY RELATION: THE ETHICAL QUESTION

Both in the case of the vendor and of the purchaser, the courts invariably declare that there would be a duty to disclose all material facts—and a correlative liability for nondisclosure—if the parties occupied a fiduciary relation toward each other.⁹⁷ As a matter of fact, quite aside from the vendor-purchaser relation, the general rule relating to the duty to disclose is stated in similar terms, viz, there is no liability for nondisclosure unless there was a duty of disclosure, and there is no duty of disclosure in the absence of a fiduciary relation. It becomes, therefore, highly relevant to inquire as to what is meant by a fiduciary relation, since liability may turn on its presence or absence. As stated in one case,⁹⁸ "Where the parties are in a confidential relationship fraud is more readily found."

Certain relationships may be called fiduciary-in-law. They are the classical relationships of trust and confidence.⁹⁹ They include, among others, attorney and client,¹⁰⁰ officers of a corporation and shareholders,¹⁰¹ joint purchasers,¹⁰² joint owners selling the jointly-owned property,¹⁰³ partner and copartner,¹⁰⁴ persons under a contract to marry,¹⁰⁵ physician and patient,¹⁰⁶ priest and parishioner,¹⁰⁷ principal and agent,¹⁰⁸ trustee and cestui que trust,¹⁰⁹ and siblings.¹¹⁰ These relations are presumed to be fiduciary, and between those who occupy them there is a

⁹⁷ "It is the duty of persons holding confidential relations, of whatever nature, with others, to put themselves on terms of perfect equality, by furnishing full, exact and truthful information of all matters which enter into a negotiation between them." *Columbus Co. v. Hurford*, 1 Neb. 146 (1871).

⁹⁸ *Keough v. St. Paul Milk Co.*, 205 Minn. 96, 285 N.W. 809 (1939). See also: *Stewart v. Phoenix Nat'l Bank*, 49 Ariz. 34, 64 P.2d 101 (1937); *Daily v. Superior Ct.*, 4 Cal. App.2d 127, 40 P.2d 936 (1935); *Goodwin v. Agassiz*, 283 Mass. 358, 186 N.E. 659 (1933); *Hockenberry v. Cooper County State Bank*, 338 Mo. 31, 88 S.W.2d 1031 (1935).

⁹⁹ See 37 C.J.S. *Fraud* § 16 (1943).

¹⁰⁰ *Gidney v. Chapple*, 26 Okla. 737, 110 Pac. 1099 (1910).

¹⁰¹ *Davis Bluff Land & Timber Co. v. Cooper*, 223 Ala. 137, 134 So. 639 (1931).

¹⁰² *Walker v. Pike County Land Co.*, 139 Fed. 609 (8th Cir. 1905).

¹⁰³ *Upton v. Weisling*, 8 Ariz. 298, 71 Pac. 917 (1903).

¹⁰⁴ *Goldsmith v. Koopman*, 152 Fed. 173 (2d Cir. 1907).

¹⁰⁵ *Costello v. Costello*, 279 N.Y. Supp. 303, 155 Misc. 28 (1934).

¹⁰⁶ *Colvin v. Warren*, 44 Ga. App. 825, 163 S.E. 268 (1932).

¹⁰⁷ *Finegan v. Theisen*, 92 Mich. 173, 52 N.W. 619 (1892).

¹⁰⁸ *Hayter v. Hudgens*, 236 S.W. 232 (Tex. Civ. App. 1921).

¹⁰⁹ *Whitesides v. Taylor*, 105 Ill. 496 (1882).

¹¹⁰ *Dolan v. Cummings* 116 App. Div. 787, 102 N. Y. Supp. 91 (1907), *aff'd*, 193 N.Y. 638, 86 N.E. 1123 (1908).

duty to make full and fair disclosure. This is not, however, to say that the courts and the authorities are unanimous as to the relationships to be included in this category. Nor does it mean that a relationship which is normally fiduciary need be so under the facts of a particular case. As a matter of fact, there is disagreement as to some relationships and, as to others, they may or may not be fiduciary, depending on the circumstances.

The partnership relation is normally deemed to be one of trust and confidence. But in one case,¹¹¹ a partner sued his copartner for fraud, alleging that the defendant induced him to sell to the other his oil leases by failing to disclose their true value. The evidence showed that the partnership relation here was strained and abnormal. Because of the strained relations they did not, said the court, enter the contract of sale "with the same confidential relations existing between them as that fixed by law."¹¹² Judgment for the victim of the alleged fraud was reversed. The court declared that "if the confidential relation fixed by law between the parties be shown . . . to have been shattered," neither party has a right to rely on the relation or "to close his eyes to the fact that he had ceased to repose that confidence in his associate [that] the law presumes to exist."¹¹³ Therefore, there was no right to rely on a full disclosure of all the material facts.

Some courts have described the fiduciary relation in broader terms than those expressed by the typical list of such relations. For example:

In law, a person occupies a fiduciary relation to another when he has knowledge and authority which he is bound to exercise for the benefit of such other person.¹¹⁴

Such a statement is undeniably true. But it is so broad as to be meaningless. It possesses the circularity of all question-begging definitions, for if it be asked when one is bound to exercise his knowledge for the benefit of another, the reply would doubtless be given: "When he occupies a fiduciary relation."

A more useful definition is that in a recent Arkansas case.¹¹⁵

The duty of disclosure also arises where one person is in (a) position to have and to exercise influence over another who reposes confidence in him whether a fiduciary relationship in the strict sense of the term exists between them or not.

The implication of this pronouncement is that the plaintiff may recover

¹¹¹ *Peckham v. Johnson*, 98 S.W.2d 408 (Tex. Civ. App. 1936), *aff'd*, 132 Tex. 148, 120 S.W.2d 786 (1938).

¹¹² *Peckham v. Johnson*, 98 S.W.2d 408, 413 (Tex. Civ. App. 1936).

¹¹³ *Ibid.*

¹¹⁴ *Whitsel v. Hoover*, 120 S.W.2d 930 (Tex. Civ. App. 1938).

¹¹⁵ *Hanson Motor Co. v. Young*, 223 Ark. 191, 196, 265 S.W.2d 501, 504 (1954).

for nondisclosure if he can show (a) that the defendant was in an influential position and (b) that the plaintiff relied. As has been shown and as will be seen further in the sequel, the courts are not nearly so liberal in imposing a duty of disclosure as this formula would indicate. One more requisite exists, viz. the plaintiff must have a *right* to rely. He cannot create the right for himself by the voluntary act of blind reliance. He must be in such a position vis-a-vis the defendant, in the light of existing circumstances, that the law *recognizes* his right to rely.¹¹⁶ By laying down this requisite, we reascend the logical "carousel" by reasking the basic question.

Some courts are cognizant of this problem of definition. One, for example, asserted that "the law is as cautious in defining a fiduciary relation in the sense which we are now using that term as it is in limiting by definition the boundaries within which fraud may be pursued."¹¹⁷

It is quite firmly established that the concept of a fiduciary relation is not limited to any arbitrary class of relations.

but there are other relations not falling in [any] of those specified classes that are in fact fiduciary. It is in each case a question of fact. The law regards the real, rather than the nominal condition.¹¹⁸

In short, in addition to the fiduciary relation "in law," there may be one "in fact."¹¹⁹ "The question is always whether or not trust is reposed."¹²⁰ And "In any case where confidence is known, or may reasonably be expected, to exist as a fact, whether it is of a legal, moral, social, domestic or personal character, equity will scrutinize the transaction critically to see that no inequitable action has been taken and no injustice has occurred."¹²¹

Lest I create the impression that mere confidence is enough, I hasten to add that "there must be something more than mere friendly relations or confidence in another's honesty and integrity. There must be something which approximates a business agency, a professional relation-

¹¹⁶ The court in *Selle v. Wrigley*, 233 Mo. App. 43, 116 S.W.2d 217, 221 (1938) states this proposition as follows: "A confidential relationship may be said to exist where two persons stand in such a relation that, while it continues, confidence is necessarily reposed by one and the influence which naturally grows out of that confidence is possessed by the other." And in *Columbus Co. v. Hurford*, 1 Neb. 146, 164 (1871), the court speaks of situations "in which confidence is *rightfully* reposed on one side and a resulting superiority and opportunity for influence is thereby created on the other." (emphasis supplied in both quotations.)

¹¹⁷ *Studybaker v. Cofield*, 159 Mo. 596, 61 S.W. 246 (1901)

¹¹⁸ *Id.* at 612, 613, 61 S.W. at 250.

¹¹⁹ *Ibid.*

¹²⁰ *Selle v. Wrigley*, 233 Mo. App. 43, 116 S.W.2d 217 (1938)

¹²¹ *Stieber v. Vanderlip*, 136 Neb. 862, 287 N.W. 773 (1939).

ship, or a family tie, something which itself impels or induces the trusting party to relax the care and vigilance which he otherwise should, or ordinarily would, exercise."¹²²

In the light of these generalizations let us examine some of the cases. It should be borne in mind that we are concerned primarily with the relationship of vendor and purchaser. But two persons who are in that relationship may simultaneously occupy one or more other relationships. Indeed, this fact may be determinative of the existence of a duty and of the actionability or nonactionability of a failure to disclose material facts. We have yet to inquire to what extent the relationship of vendor and purchaser may in itself be considered fiduciary in nature.

A lessor sued his lessee, under an oil lease, for fraud in accounting for profits. The trial court found that the plaintiff had "implicit faith" in the honesty and integrity of the defendant, but held that "this was not sufficient to make out a fiduciary relationship."¹²³

A patient had voluntarily entered a mental hospital. Subsequently he expressed a desire to be released, and the hospital failed to inform him that he could secure a release upon a written order. He sued for false imprisonment. The court held that the relationship was not such as would render fraudulent a failure to disclose.¹²⁴ If the general statements quoted earlier have any significance, the result in this case is unsound. Surely a patient has a right to rely on a hospital for a full disclosure of all facts which would be of importance to him, provided that possession of the facts would not be harmful to him.

A Texas court found no fiduciary relation to exist between the temporary administrator of a decedent's estate and the collateral heirs of the decedent.¹²⁵

In another case,¹²⁶ the defendant bought and sold bonds for the plaintiff for thirty years, the transactions involving, in all, several millions of dollars. The plaintiff sued for fraud, alleging that the defendant failed to disclose to him material facts about the state of the markets. *Held*, judgment for the defendant. There was no fiduciary relationship between the parties despite the long history of their transactions and the many

¹²² *Collins v. Nelson*, 193 Wash. 334, 75 P.2d 570 (1938). Another court stated the proposition in the following terms: "Confidential relation is not confined to any specific association of the parties. It appears when the circumstances make it certain the parties do not deal on equal terms, but, on the one side there is an overmastering influence, or, on the other, weakness, dependence, or trust, justifiably reposed." *Leedom v. Palmer*, 274 Pa. 22, 117 Atl. 410 (1922).

¹²³ *Fowler v. Associated Oil Co.*, 74 P.2d 727 (Cal. 1937).

¹²⁴ *Roberts v. Paine*, 124 Conn. 170, 199 Atl. 112 (1938).

¹²⁵ *Whitsel v. Hoover*, 120 S.W.2d 930 (Tex. Civ. App. 1938).

¹²⁶ *Harrison v. Welsh*, 295 Pa. 501, 145 Atl. 507 (1929).

expressions of confidence and reliance by the plaintiff upon the service or judgment of the defendant. Although the vendor had a better opportunity to acquire knowledge as to the value of the subject matter of the sale, the facts were discoverable by the purchaser. Hence, there was no duty of disclosure. This case represents a fairly strict attitude and an unwillingness to find that trust existed as a fact where the relationship, although intimate and long-lasting, was essentially no more than one of vendor and purchaser.

There is one class of cases in which there is considerable conflict in the decisions as to the existence of a fiduciary relationship, viz. those involving promoters, directors or officers of a corporation on the one hand and shareholders or prospective shareholders on the other. The existence of this conflict is symptomatic, in this instance, of a transitional stage in the law, for there can be no doubt that the concept that directors and other "insiders" stand in some sort of position of trust as to the "outsiders" is gaining in favor. It has been many times stated that as a general rule a director or officer does not occupy a fiduciary relation toward a shareholder,¹²⁷ although that rule has been undergoing steady attrition.¹²⁸

But even the fairly early cases recognized that special circumstances may exist which impose a duty to disclose facts regarding corporate affairs affecting the value of the stock. In a Canadian case,¹²⁹ for example, where the managing officers of a corporation concealed the fact that, as a committee appointed for the purpose, they had sold corporate property at a price which greatly enhanced the value of the corporate stock and bought in the stock at the lower value, the officers were liable to the seller, since, under the circumstances, the information was received in a fiduciary capacity.

Many cases state that the directors do not stand in a fiduciary relation when dealing with shareholders for the purchase or sale of stock (though they may occupy a fiduciary relation to the corporation) and in order to constitute fraud in such a case there must be actual misrepresentation.¹³⁰ A fortiori, where both of the parties to the purchase and sale of corporate stock are officers and directors of a corporation, neither owes the other any special duty of a fiduciary nature, and the sale will not be set aside because of the purchaser's failure to disclose all the facts within his

¹²⁷ See cases collected in 84 A.L.R. 615, 623 et seq. (1933).

¹²⁸ Note, *Fiduciary Obligations of Controlling Shareholders*, 7 WEST. RES. L. REV. 467 (1956).

¹²⁹ *Gadseen v. Bennette*, 23 Man. L. Rep. 33, 9 D.L.R. 719 (1913).

¹³⁰ *Buckley v. Buckley*, 230 Mich. 504, 202 N.W. 955 (1925). One case states that if the shareholder actually relies, the director must make full disclosure. *George v. Ford*, 36 App. D.C. 315 (1911).

knowledge bearing on the value of the stock. The result is not changed by the fact that at the time of the purchase, the stock is worth much more than the price paid.¹³¹

If, on the other hand, the shareholder makes inquiries, the officers and directors, dealing with him for the purchase of his stock must reveal fully and truthfully the facts concerning the financial condition of the company, the value of the stock, the probability of dividends, future plans, etc.¹³²

*Lovell v. Smith*¹³³ is a fairly extreme but not entirely typical example of the cases which impose no duty of disclosure. The defendants, promoters of a corporation, did not disclose in their prospectus the fact that they had secured their stock on more advantageous terms than those on which it was being offered to the public, and the plaintiff. Nor did they disclose that they had procured, at the outset, voting control over the company. The trial court found no statements in the prospectus which were fraudulent or calculated to deceive the plaintiff. The court found no fraud, no fiduciary relation and no duty to disclose. Judgment for the defendants was affirmed. There are, on the other hand, cases, especially recent cases, which hold that directors and officers occupy a fiduciary relationship to the shareholders, imposing a duty to disclose all material facts and declaring that silence amounts to fraud.¹³⁴

An extreme representative of these cases is *Hotchkiss v. Fischer*¹³⁵ where, it was held that a director who purchases on his own account a shareholder's shares acts in a relation of "scrupulous trust and confidence," is required to deal with the utmost fairness and to communicate fully to the shareholder all material facts bearing on the transaction, which he knows or which, because of his position, he should know. A shareholder was permitted to recover damages for the director's failure to make full disclosure even though the defendant furnished the plaintiff with a statement which fully explained and fairly showed the true financial condition of the company and, in addition, answered truthfully such questions as the plaintiff asked and offered to give any further requested information within his knowledge. The nondisclosure lay in the fact that the financial statement did not, without interpretation, disclose the real financial condition of the company.

Other cases¹³⁶ take a similar, if less extreme, point of view, and one

¹³¹ *Hallidie v. First Federal Trust Co.*, 177 Cal. 600, 171 Pac. 431 (1918).

¹³² *Waller v. Hodge*, 214 Ky. 705, 283 S.W. 1047 (1926).

¹³³ 232 Ala. 626, 169 So. 280 (1936).

¹³⁴ *Carr Consol. Biscuit Co. v. Moore*, 125 F. Supp. 423 (M.D. Pa. 1954).

¹³⁵ 136 Kan. 530, 16 P.2d 531 (1932).

¹³⁶ See, e.g. *Markey v. Hibernia Homestead Ass'n*, 186 So. 757 (La. App. 1939).

of them sums the matter up by stating that there is at least a "quasi-fiduciary connection" between a stockholder and the officers or directors of a corporation. The modern trend is in favor of this viewpoint.

Many other relations have been held to be fiduciary in character under the facts of a particular case.

The director of a children's camp, for example, was recently held liable in fraud to the parents of a camper for his failure to fully disclose the facts concerning the dispensary and infirmary facilities. The court stated that the defendant occupied "a position similar to one in a fiduciary relation wherein nondisclosure is recognized as the basis for fraud."¹³⁷

A general contractor was held liable for not disclosing his failure to use the type of roofing materials stipulated for.¹³⁸ The executor of a decedent's estate was held to owe the remainderman the highest degree of fidelity and, in obtaining the latter's signature to a deed conveying his interest to the executor, the executor had a duty to disclose, fully and fairly, all pertinent facts. His failure to do so amounted to fraud as a matter of law (good faith was immaterial) and entitled the remainderman to a cancellation of the deed.¹³⁹

In an interesting Missouri case,¹⁴⁰ the purchaser of a deed of trust sued to recover damages for misrepresentation from the defendant real estate company. The plaintiff was allowed to recover although there were no affirmative representations as to the existence of tax liens against the property. The court found a fiduciary relation to exist and held, accordingly, that the defendant owed to the plaintiff, its client, "something more than mere silence on the important question of the condition of the property with respect to taxes thereon."¹⁴¹ The court stressed the fact that that the company was experienced in such business, that its officers knew

Here the plaintiff sued for fraud, alleging that the defendant association induced her to sell her shares of defendant's capital stock to it at a discount. The association failed to advise the shareholder that it intended to renew its rejected application to the Federal Savings and Loan Insurance Corporation for insurance on its stock. This, felt the court, warranted an inference of intentional concealment and bad faith. Judgment for the defendant on demurrer was reversed. See also *Heckscher v. Edenborn*, 203 N.Y. 210, 96 N.E. 441 (1911) in which the defendant promoter of a syndicate was held to be under a duty to give information of his interest. Failure to do so was held to be fraud, entitling the other parties to rescind the syndicate agreement. The court stressed the "rather intimate and influential relations" which existed.

¹³⁷ *Schlenoff v. Kroll*, 207 Misc. 1082, 141 N.Y.S.2d 370 (1955). Plaintiff, however, could not recover in fraud because he had elected to rescind.

¹³⁸ *Ruebeck v. Hunt*, 171 S.W.2d 895 (Tex. Civ. App. 1943), *aff'd*, 142 Tex. 167, 176 S.W.2d 738 (1943). Fraud was relied on because of the statute of limitations.

¹³⁹ *Murphy v. Cartwright*, 202 F.2d 71 (5th Cir. 1953). The executor failed to disclose the value or extent of the estate.

¹⁴⁰ *Klika v. Wenzlick Real Estate Co.*, 150 S.W.2d 18 (Mo. App. 1941).

¹⁴¹ *Id.* at 23.

that the plaintiff was not experienced and that in her lack of experience, plaintiff "had a right to repose complete confidence" in the agent of the defendant, and was justified in expecting full disclosure.

*Chandler v. Butler*¹⁴² was an action by a seller of stock for damages allegedly suffered as a result of fraudulent representations as to the value of the stock by the purchaser. There were no actual, verbal representations. In finding a relation of trust and in holding for the plaintiff, the court emphasized the seller's advanced age, his lack of knowledge as to the fair market value of his stock, the purchaser's knowledge of this ignorance and of the fact that the plaintiff was trusting the purchaser to deal fairly. They were not, said the court, dealing at arm's length, and the defendant therefore had a duty to speak and no right to evade, conceal, mislead or overreach the seller.

Other examples of a fiduciary relation "in fact," are presented in the s.¹⁴³

Many of the cases just discussed involved vendors and purchasers. We turn now to our final inquiry: Is the vendor-purchaser relationship (in the absence of any other special relations) inherently fiduciary, either in law or in fact?

Clearly, the vendor-purchaser relation is not within that class of relations which the law has traditionally regarded as fiduciary in character. This point is borne out by the many cases discussed and cited in the sections dealing with the duties of the vendor and of the purchaser. It is further emphasized by the following statements:

The relation of the parties was *merely* that of buyer and seller not affected by any fiduciary obligations.¹⁴⁴ (emphasis supplied)

The parties here were dealing at arm's length, the usual situation of

¹⁴² 284 S.W.2d 388 (Tex. Civ. App. 1955).

¹⁴³ In *Trout v. Harrell*, 217 Ark. 670, 676, 233 S.W.2d 233, 236 (1950) the plaintiff sought to cancel a deed which she alleged was obtained from her by the fraud of the defendant, her step-son. The court declared that "the mere relationship of step-mother and step-son does not, *ipso facto*, create a confidential relationship in all the dealings between the parties. Likewise, the mere relationship of cotenancy does not, *ipso facto*, create a confidential relationship in all the dealings between the parties, even though such a relationship may exist in some matters." But rescission was allowed because the defendant, in answering the plaintiff's questions, was evasive and equivocal, and the court felt that plaintiff in fact, did rely on the answers.

In *Gardner v. Nash*, 225 S.C. 303, 82 S.E.2d 123 (1954) the defendant knowingly allowed the impression to exist that he was bidding in for the mortgagor at a foreclosure sale, with the result that the bidding was "chilled." He then refused to convey to the mortgagor. Held, the failure to speak, under the circumstances, amounted to the suppression of a fact which should have been disclosed, and constituted a fraud.

¹⁴⁴ *Noved Realty Co. v. A. A. P. Co.*, 250 App. Div. 1, 293 N.Y. Supp. 336 (1937).

vendor and purchaser; neither trusted the other; each sought to gain all the advantage possible.¹⁴⁵

And in a case in which a fiduciary relation *was* found to exist, the court took pains to point out that "he [the vendor] did not occupy the position of an *ordinary vendor*, but he was inviting others to confer upon him a fiduciary relationship."¹⁴⁶ (emphasis supplied) The implication is clear, that the "ordinary vendor" does not occupy a fiduciary position.

If the vendor and the purchaser did occupy such a position toward each other, then each would have a duty of full disclosure and a corresponding right to rely on disclosure by the other. The question whether a fiduciary relation exists could be formulated in different terms: Do they have a *right* to rely? And this question, once we accept the proposition that there may exist relations fiduciary-in-fact, distills into a factual question: Do vendors and purchasers *in fact* rely on each other for full and fair disclosure? If they do as a matter of practice, then they have a right to do so and a de facto fiduciary relationship arises.¹⁴⁷ This conclusion is reached in the following manner: If the parties in fact rely, as a matter of general custom and practice, then each must be held to know that he is being relied upon. He is thus placed under a *duty* to justify that reliance. Ergo, he is in a position of trust and confidence with which his conduct must comport. He *is* a fiduciary.

Those cases which have predicated liability upon nondisclosure have done so on one of two grounds. Either they have found that in addition to the vendor-purchaser relation, another relation of trust subsisted between the parties; or they have found (this is usually implicit in the decision rather than express) that vendors and purchaser do rely, that each knows that the other relies, that custom sanctions the reliance and that this results in the creation of a duty not to frustrate the confidence thus reposed by failure to disclose material facts.

¹⁴⁵ *Greenberg v. Glickman*, 50 N.Y.S.2d 489 (1944), *immaterially modified*, 268 App. Div. 882, 51 N.Y.S.2d 96 (1945), *appeal denied*, 268 App. Div. 987, 51 N.Y.S.2d 861 (1945).

¹⁴⁶ It may be helpful in this regard not to generalize about the vendor-purchaser relation. There would seem to be a distinction between the relationship, on the one hand, of two experienced business men, consummating a sale and purchase and the relationship, on the other, of salesman and customer in a large retail store. To the former, the description "arm's length" seems to be appropriate, and there is little ground for reliance, except to the extent of warranties and of unequivocal representations of fact. But in the latter, it may be doubted whether it is ever possible for the parties to achieve equality of knowledge. And while the customer may be held to act at his peril in relying on statements which he should recognize to be customary "sales talk," it can be argued that he relies, and justifiably so, on the sales person not to remain silent as to material facts of which he knows the purchaser is ignorant.

¹⁴⁷ This would be so unless there were some overmastering social or economic reason to deny recognition to the de facto relation.

Most courts evidently believe that in the world of business transactions, men are "rugged individualists," that even scrupulously honest men who would not affirmatively suppress or conceal the facts, are willing to exploit their superior knowledge of the facts by failing to make a gratuitous disclosure to the other party.

Let us assume that this is an accurate appraisal of business ethics as they exist in our society. The next question is whether this is a desirable state of affairs. It is, then the majority of courts are correct in denying a remedy for "mere silence." But let us assume, *arguendo*, that it is morally reprehensible for a vendor not to disclose to his purchaser (and, of course, vice versa) facts, known to the one and not to the other, which if known to the other, would materially affect his conduct with respect to the transaction. Let us suppose that it could be shown that such a rule of conduct is morally degrading and that it is, in effect, no different and no less deplorable than active fraud and deceit, which are clearly beyond the pale. These suppositions do not settle the matter. There are many areas in which human conduct falls short of the standards demanded by a high sense of morality.¹⁴⁸ Does the law in each such area use its powers of restraint and of coercion to enforce adherence to the dictates of morality? Should it? Can it? This is the heart of the problem: Is it the function of the law to elevate man morally, to "improve" his social behavior and to set an ethical norm which is higher than the existing mores and standards of society? Or should the law content itself with reflecting and enforcing the moral norms of society as they are?

Much has been written and will be written on this question, for it is a complex and profound one, and it has a direct bearing not only on the subject under consideration but on many of the unresolved problems in the field of torts. After all, the first and central substantive question in tort law as to any pattern of behavior is always: Is this a wrong? Although the question may be asked in varying forms: Was the defendant under a duty? Did the plaintiff have a right? — the essence of the question does not change. And the answer invariably depends on the broader question of whether the law is to be an active and creative force in shaping man's social behavior or a passive reflector and applier of the accepted standards. This is the underlying question in the field of fraudulent non-disclosure as much as in any other tort problem. And it is no less so merely because the courts tend to ignore it. Most judges are not social philosophers.

¹⁴⁸ One scholar, at least, believes that "people must satisfy their ethical feelings by laying down a moral rule, while they actually live on a lower grade of morality." Page, *Professor Ehrlich's Czarnowitz Seminar of Living Law*, HANDBOOK OF THE ASS'N. OF AMER. LAW SCHOOLS 46 (1914), as quoted in 22 B.U.L. REV. 607, 609 (1942).

Yet indirectly their decisions on the so-called "questions of law" imply an answer to the broader questions of legal philosophy. And, whether expressly or not, decision in those areas of law which, like the one under consideration, are really permeated with moral questions, reflect the moral judgment of the court. If a failure to disclose is, under the particular facts, shocking enough to the moral sense, relief will be granted. If it falls short of this effect, the courts will say that whatever the status of the defendant's conduct in the "forum of the conscience" it is not actionable in the forum of the law.

Many cases demonstrate that the courts *are* concerned with honesty and morality. One speaks of "honesty and good faith" as that which requires disclosure.¹⁴⁹ Another speaks of "common honesty and fair dealing."¹⁵⁰ And, when, as often happens, the ultimate task of deciding whether there was a fraud, is assigned to the jury, the members of that body (except to the extent that they are effectively limited by the court's instructions) will surely apply their own moral standards in deciding whether the defendant's conduct was sufficiently reprehensible to justify giving the plaintiff relief.¹⁵¹

It has been said that there has been a shift in business ethics from a period in which reliance was hardly ever justified and when one could assume that the other party would overreach, to one in which there prevails a new and higher standard.¹⁵² Others have said that the doctrine of caveat emptor has lost much of its content.¹⁵³ Without evaluating the accuracy of these observations, one may safely conclude that they possess some basis, and that both judge and jury, try as they might to objectify their attitudes, are sensitive at least to the grosser changes in business ethics. The question here is how high an ethical standard will be demanded. Or, stated differently, how much of a premium will be placed on shrewdness and astute bargaining skill, either of the vendor or the purchaser, which falls short of active concealment or clear misrepresentation? Like many other legal questions, it is fundamentally an ethical and social question. The answer is still being formulated, and since the law, though gradual, is not static, the process of formulation will be endless.

¹⁴⁹ *Lovell v. Smith*, 232 Ala. 626, 169 So. 280 (1936).

¹⁵⁰ *Weiland v. Turkelson*, 38 N.J. Super. 239, 118 A.2d 689 (1955).

¹⁵¹ At least one writer believes that the question whether the particular nondisclosure is actionable is one properly in the province of the court. Yet the same writer declares that the standard of fair conduct is that of the "ordinary ethical person." This would seem to require the type of *factual* determination which, in our jurisprudence, has traditionally been the prerogative of the jury. Keeton, *Fraud-Concealment and Non-disclosure*, 15 TEX. L. REV. 1 (1936)

¹⁵² PROSSER, *TORTS* 552 et seq. (2d ed. 1955).

¹⁵³ Keeton, *op cit. supra* note 151.

SUMMARY AND CONCLUSION

It is always dangerous, in any area of the law, to make statements which even approach absolutism. There is hardly a rule which does not have exceptions and the enunciation of which, if unqualified, would not be misleading. Yet there is an advantage in placing a rule in rather sharp focus, and in bringing out its essential outlines, unconcerned for the moment, with the nuances and detail. The attempt to hedge, to be cautious, to include the circumstances which qualify its application within the formula itself results, often as not, in a fuzzy statement and an unwieldy instrumentality. Most of the cases and the writers, including the writers of the various applicable Restatements, seem to be overly afraid of the definite formulation.

Fully aware of the dangers of generalization and of the importance of knowing the exceptions, this writer is willing to state that in the typical transaction, nondisclosure of material facts on the part of a vendor or purchaser is not fraudulent. This is the older law, and, notwithstanding a movement in the other direction, manifested by the gradual multiplication of qualifying exceptions, it is the modern law as well.

Special circumstances will change the result. If, for example, the facts are such that another, a classically fiduciary relationship exists, or if there is an extremely strong reason to justify the reposing of trust and confidence, and it is, in fact, reposed, the law will impose a duty of disclosure. If the facts are *exclusively* in the possession of one party and absolutely inaccessible to the other, the same result may occur.¹⁵⁴ If the undisclosed fact is of the existence of a latent defect in real property, many courts impose liability for the nondisclosure, especially if the vendor created the condition or if it is dangerous to health or safety. If, something is said, and what is left unsaid would qualify it absolutely, the nondisclosure will be actionable. If questions are asked, and evasive or half-true answers are given, this may be fraud. If affirmative acts of concealment are indulged in, they will be deemed equivalent to verbal misrepresentations.¹⁵⁵ If the implication of silence, in the light of surrounding circumstances, is to falsely represent the existence or nonexistence of a fact, the silence will be deemed wrongful. If conditions have changed since an affirmative representation, true when made, was made, the maker may be under a duty to speak. And finally, if the conscience of the court, which is at least to a substantial degree, the

¹⁵⁴ See dictum in *Everett v. Gilliland*, 47 N.M. 269, 141 P.2d 326 (1943). The courts *speak* in terms of *reasonable* inaccessibility but seem to *act* in terms of *absolute* inaccessibility.

¹⁵⁵ *Stewart v. Wyoming Cattle Ranch Co.*, 128 U.S. 383 (1888)

archetype of the conscience of the community, is sufficiently stirred, relief will be given.

In our culture, to date, passive concealment is generally not considered immoral or fraudulent. Accordingly, for the cautious vendor or the diligent purchaser who has a monopoly of the material facts, silence is truly golden. And only if rather special circumstances are found to exist, will the law enact its penalty and hold that silence was fool's gold.