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THE COLLISION OF TORT AND CONTRACT IN THE CONSTRUCTION INDUSTRY

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INTRODUCTION

Over the last twenty years, attorneys representing construction industry clients have been participating with increasing vigor in what Dean Prosser called the "more or less inevitable efforts . . . to turn every breach of contract into a tort."[1] Construction lawyers have attempted to turn ordinary economic loss[2] claims normally governed by contract, such as claims for damages due to delayed or disrupted work, into negligence actions against parties with whom their clients have no contractual relationship. For example, many general contractors who have been damaged by delayed work now file negligence claims against project architects instead of (or in addition to) contract claims against the owner with whom the builder has contracted. Moreover, many times when builders assert traditional contract claims against owners, they also assert a negligence claim on the same issue.

There are many factors that attract attorneys and their clients to the tort arena. Generally, consequential damages are recovered more easily in negligence claims than in contract claims. In addition, tort law holds out the prospect of numerous defendants while

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1. W. PROSSER & W. KEETON, THE LAW OF TORTS § 92, at 658 (5th ed. 1984).

2. "Economic loss," as the term is used in this article, includes damages for inadequate value, repair and replacement costs, lost profits and the increased cost of performing work. In the construction context, economic losses often include the additional cost of completing the work due to delays or disruptions. For a discussion of the term, see Moorman Mfg. Co. v. National Tank Co., 91 Ill. 2d 69, ___, 435 N.E.2d 443, 449 (1982).

a contract action may be asserted only against a contract partner. For example, an aggrieved subcontractor might assert negligence claims against the owner, the project architect, and one or more engineers in addition to the general contractor, who is the only entity with whom the subcontractor has a contract. The rationale is that more defendants will mean more money available for the settlement pot. Since many complex construction cases are settled before trial, the possibility of additional settlement participants is alluring.

Probably a more compelling motivation to assert a negligence claim is the desire to escape contract provisions which restrict potential recoveries from the privity partner. Construction contracts often include provisions limiting or precluding recovery of damages for delay, requiring notice of claims, and limiting the amount of overhead and profit recoverable. Where such provisions apply, a negligence claim is more likely to produce a satisfactory result for the plaintiff.

Until recently, the different principles underlying negligence and contract law have thwarted attempts to turn construction contract breaches into negligence claims. However, the appeal of applying negligence principles to construction contract disputes has led some courts to permit negligence claims. The process has been fueled by the elimination of the privity defense in personal injury and property damage cases. Some courts have reasoned that if the privity defense is eliminated for some actions it should be eliminated for all. Yet these decisions fail to recognize that contract and tort law have fundamentally different roots and functions. These differences make negligence analysis inappropriate when applied to cases involving purely economic losses.

This article first reviews the different origins and purposes of negligence and contract law. The article then focuses on the standard of liability in the construction industry and the troubling development of the rule that purely economic losses may be recovered in negligence. Finally, the article analyzes recent decisions from the products liability and construction fields reflecting an emerging trend away from allowing negligence actions for economic losses.

While this article focuses on the construction industry, the principle that contract law should govern business disputes involving purely economic losses applies to commercial transactions generally.

I. A Historical Look at Negligence and Breach of Contract

A. *The Concept of Negligence*

The cause of action for negligence developed at English common law as an extension of the doctrine of trespass. Under the form of action trespass *quare clausum fregit*, a plaintiff was entitled to recover damages occasioned as a result of an unlawful entry upon his land.[3] Trespass on the case extended the doctrine beyond the close of the plaintiff's real estate and protected his person and property.[4] As the lineal descendant of trespass on the case, the negligence cause of action evolved to redress losses occasioned by personal injury, wrongful death, and injury to both real and personal property.

To establish a prima facie case in negligence, the plaintiff must prove a duty owed by the defendant to him, a breach of that duty, and damages proximately resulting from the breach.[5] Negligence is "[t]he omission to do something which a reasonable man, guided by those ordinary considerations which ordinarily regulate human affairs, would do, or the doing of something which a reasonable and prudent man would not do."[6] What seems reasonable to the person in question is not at issue. This duty to act reasonably is an objective standard of acceptable conduct imposed by society. It exists in the absence of any agreement between the parties and is imposed whether or not the parties were aware of the duty. The duty is owed to all who might foreseeably suffer injury as a result of its breach.[7]

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3. Black's Law Dictionary 1119 (5th ed. 1979). *See also* 3 T. Street, The Foundations of Legal Liability 232-33 (1906).

4. 2 F. Harper & F. James, *The Law of Torts* § 12.3, at 749-50 (1956).

5. Atlantic Co. v. Morrisette, 198 Va. 332, 333, 94 S.E.2d 220, 221-22 (1956).

6. Black's Law Dictionary 930 (5th ed. 1979); *see* Perlin v. Chappell, 198 Va. 861, 864, 96 S.E.2d 805, 808 (1957) (quoting Montgomery Ward & Co. v. Young, 195 Va. 671, 673, 79 S.E.2d 858, 859 (1954) ("The test is that degree of care which an ordinarily prudent person would exercise under the same or similar circumstances to avoid injury to another.")). Where society has dealt with standards of conduct by enacting criminal statutes and ordinances, the statutory standards take the place of the reasonable man test. *See, e.g.*, Butler v. Friedan, 208 Va. 352, 353, 158 S.E.2d 121, 122 (1967) (violation of ordinance prohibiting unleashed dogs constitutes negligence *per se*).

7. *See* Virginia Elec. & Power Co. v. Savoy Constr. Co., 224 Va. 36, 46, 294 S.E.2d 811, 818 (1982) (quoting New Bay Shore Corp. v. Lewis, 193 Va. 400, 409, 69 S.E.2d 320, 326 (1952) (proximate cause does not require that the "precise occurrence be foreseen, but only that a reasonably prudent person under similar circumstances ought to have anticipated

The public policy behind the law of negligence is that society imposes upon all of its members certain norms of behavior to the end that others will not be injured or have their possessions destroyed or damaged. In the event that the norms are violated and an injury results, society shifts the losses, both direct and consequential, from the injured party to the party at fault.

The compensation goal of tort law is reflected in the liberal rules of tort damages. A negligence victim is entitled to recover for both the direct and consequential losses proximately caused by the breach of duty.[8] There are some limitations on tort damages. For example, consequential damages generally are not recoverable in the absence of some physical injury.[9] However, given proof of a physical injury and direct damages flowing from it, plaintiffs have been entitled to recover for associated losses, including an array of economic losses.[10] Even unforeseeable damages normally are recoverable in negligence. For example, a tortfeasor is liable for aggravated damages caused by negligent medical treatment of injuries.[11]

B. *The Concept of Breach of Contract*

While the negligence cause of action developed to shift the cost of accidents to the responsible party, the law of contracts evolved to enforce agreements between members of society. The efficient operation of a market economy requires that people be free to agree with others as they see fit, and that their agreements be enforced according to their terms.[12] The aim of contract law is simply

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'that an injury might probably result from the negligent acts' ")).

8. The Restatement states the rule as follows: "One who tortiously harms the person or property of another is subject to liability for damages for the consequences of the harm in accordance with the rules on whether the conduct is a legal cause of the consequences." RESTATEMENT (SECOND) OF TORTS § 917 (1979). Comment d of Section 917 contrasts the damages normally recoverable in tort and contract. *Id.*

9. *See, e.g.*, Womack v. Eldridge, 215 Va. 338, 342, 210 S.E.2d 145, 148 (1974) (recovery allowed for emotional distress unaccompanied by physical injury only where conduct is intentional or reckless, offends the generally accepted standards of decency and morality, and the emotional distress is severe). *But cf.* Naccash v. Burger, 223 Va. 406, 290 S.E.2d 825 (1982) (recovery for emotional distress permitted in "wrongful birth" case).

10. RESTATEMENT (SECOND) OF TORTS § 924 (1979).

11. Corbett v. Clarke, 187 Va. 222, 224-25, 46 S.E.2d 327, 328 (1948); *see also* Powell v. Troland, 212 Va. 205, 212, 183 S.E.2d 184, 188 (1971) (aggravated damages caused by negligent medical care awarded to plaintiff injured in automobile collision).

12. On the role of the state as enforcer of contracts, see T. HOBBES, LEVIATHAN 196-203 (Penguin ed. 1968). Adam Smith observed that "[w]hen the law does not enforce the performance of contracts . . . . [t]he uncertainty of recovering his money makes the lender exact the same usurious interest which is usually required from bankrupts." A. SMITH, AN

to give the parties to a contract the benefit of their bargain and, in the event of breach, to put the injured party in as good a position as if performance had been rendered as promised.[13]

In commercial transactions, the parties establish the terms of their agreements. The parties assume certain risks and anticipate certain rewards based upon their knowledge, goals and relative bargaining power. The duties of each party are reflected in the contract governing the transaction. In the event of a breach, the terms and conditions of the contract become the law of the case.[14] Judges are not empowered to modify or add to the parties' agreement.[15] In interpreting an ambiguous provision, a judge's task is not to determine what would have been reasonable but rather to determine what the parties actually meant.[16] Similarly, jurors are not permitted to make a new contract for the parties by deciding what is "fair," but are asked only to make findings of fact which will enforce the agreement the parties made for themselves.[17]

The social policy underlying contract law is to preserve the efficiency of the free market. This goal is accomplished by assuring to all contracting parties the benefits and burdens of the agreements voluntarily assumed by them.

The different roots of negligence and contract law are reflected in contrasting rules for contract and negligence claims. For example, the source of contractual duties is the agreement between the parties rather than general obligations imposed by society (*i.e.*, the duty to act reasonably). Even contractual terms which are objectively unreasonable will be enforced. For example, under the Uniform Commercial Code (the UCC) performance is excused by a supervening occurrence which alters a basic assumption of the

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INQUIRY INTO THE NATURE AND CAUSES OF THE WEALTH OF NATIONS 40 (Encyclopedia Britannica ed. 1975).

13. 5 A. CORBIN, CONTRACTS § 992, at 5-7 (1964).

14. Winn v. Aleda Constr. Co., 227 Va. 304, 307, 315 S.E.2d 193, 194-95 (1984) (court enforced construction contract's requirements that covenants be "*strictly* performed" and building be "*fully* completed") (emphasis in original).

15. Stonega Coal & Coke Co. v. Louisville & Nashville R.R., 106 Va. 223, 226-27, 55 S.E. 551, 552 (1906).

16. *Id.* at 227, 55 S.E. at 552.

17. *See, e.g.*, Rhodes v. National Homes Corp., 263 S.E.2d 84 (W. Va. 1979); *cf.* Greater Richmond Civic Recreation, Inc. v. A.H. Ewing's Sons, Inc., 200 Va. 593, 596, 106 S.E.2d 595, 597 (1959) (where a contract is ambigious in its terms and unclear on its face and it is necessary to resort to parol evidence to ascertain the intention of the parties, construction of the contract may be a jury question).

contract and renders performance commercially impractical.[18] However, as the drafters of the UCC noted, the impracticality excuse may be "expressly negated by the language of the agreement."[19] Thus, if the parties wish, their agreement, not a judge's concept of "impracticality," will govern their relationship.

Another important difference between tort and contract is the "right to breach." Normally one has a right to end a contractual relationship, recognizing that the other party is entitled to be placed in the same economic position he would have occupied had the contract been performed. Only under special circumstances may an aggrieved party obtain specific enforcement of a contract.[20] Moreover, punitive damages are not normally recoverable in contract actions.[21] No corresponding "right to breach" exists under tort law. Intentional torts give rise to additional penalties beyond damages suffered.[22]

The general rule of contract damages is that consequential damages are not recoverable unless they were within the contemplation of the parties at the time of contracting and became a basis for the bargain.[23] In contrast, consequential damages generally are recoverable in negligence actions.[24]

II. The Standard for Contractual Liability in the Construction Industry

The performance of contractual duties by design professionals[25] is subject to a reasonableness standard similar to the general negligence duty. Design professionals generally do not guarantee their plans and specifications, but they promise (often implicitly) that they will exercise reasonable care in performing their work. Since

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18. Va. Code Ann. § 8.2-615(a) (Added Vol. 1965).

19. *Id.* § 8.2-615, official comment 8.

20. D. Dobbs, Handbook on the Law of Remedies § 12.2, at 795-97 (1973).

21. Kamlar Corp. v. Haley, 224 Va. 699, 706, 299 S.E.2d 514, 517-18 (1983) (proof of an independent, willful tort, beyond the mere breach of a duty imposed by contract is required for an award of punitive damages in a contract case, regardless of the motive for the breach).

22. *E.g.*, punitive damages and, in some circumstances, the penalties imposed by the criminal law. The additional disincentives associated with the intentional breach of tort duties reflect the public safety policy underlying tort law.

23. Hadley v. Baxendale, 156 Eng. Rep. 145 (Ex. 1854).

24. *See supra* notes 8 & 9 and accompanying text.

25. The term "design professionals" is used in this article to refer to architects and engineers.

design professionals and their clients are free to determine the terms of their agreements, design contracts occasionally include language that may be interpreted as a guarantee of a workable design.[26] Such agreements, however, are unusual.

Builders are held to a similar standard. Absent a contrary contractual provision, their work must be "reasonably good and workmanlike" and "reasonably fit for the intended purpose," but need not be perfect.[27] Of course, builders are also free to agree to a higher obligation in their contracts.[28]

The "reasonable care" and "workmanlike" standards are sensible given the imprecise nature of building design and construction, but they tend to blur the line between contract and tort. In *Surf Realty Corp. v. Standing*,[29] a leading design professional liability case, the court employed language usually associated with negligence cases to describe a design professional's obligations. *Surf Realty* involved a claim against an architect arising out of the design and construction of a rolling roof for a dance hall. The owner was dissatisfied with the resulting construction and refused to pay the architect his fee. The Supreme Court of Virginia decided that there were no implied warranties in connection with the architect's services, but that a design professional, in his contract of employment, "implies that he possesses the necessary competency and ability, to enable him to furnish plans and specifications prepared with a reasonable degree of technical skill."[30] The court ruled that an architect "must possess and exercise the care of those ordinarily skilled in the business and, in the absence of a special agreement, he is not liable for fault in construction resulting from defects in the plans because he does not imply or guarantee a perfect plan or a satisfactory result."[31] The rule is the same throughout the United States.[32]

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26. *See, e.g.*, Hill v. Polar Pantries, 219 S.C. 263, 64 S.E.2d 885 (1951) (design contract containing terms such as "adequately serve the needs" and "necessary controls and equipment" led court to impose guarantee obligation on designer).

27. Mann v. Clowser, 190 Va. 887, 901, 59 S.E.2d 78, 84 (1950).

28. For example, the builder in Lambert v. Jenkins, agreed that his work would be "first class and satisfactory in every respect." 112 Va. 376, 377, 71 S.E. 718, 719 (1911); *see also* Winn v. Aleda Constr. Co., 227 Va. 304, 307-08, 315 S.E.2d 193, 195 (1984) (building contract required the builder to perform the contractual requirements "strictly").

29. 195 Va. 431, 78 S.E.2d 901 (1953).

30. *Id.* at 442-43, 78 S.E.2d at 907.

31. *Id.* at 443, 78 S.E.2d at 907.

32. *See, e.g.*, Looker v. Gulf Coast Fair, 203 Ala. 42, ___, 81 So. 832, 835 (1919) ("A competent architect, pursuing an independent profession, is not an insurer of the accuracy or

Based on the reasonableness standard, the court in *Surf Realty* upheld the trial court's finding that, despite serious problems with the project, the architect had not breached the implied condition of his contract. The court also ruled, however, that the architect had breached his construction supervision duties in several respects.[33]

Surf Realty involved an owner's claim for economic loss. The architect's contract for services did not contain provisions defining the standard by which the architect's performance would be judged. As a result, the court found that a standard was implied as a condition of the contract. A breach of the implied condition would have had the same effect as the breach of any other condition; the owner would obtain judgment for the "benefit of his bargain."[34]

In addition to their contractual duties to their clients, design professionals owe a tort duty to the general public to take reasonable care to avoid causing foreseeable personal injuries or property damage.[35] Although violation of this tort duty is not conceptually different from any other negligence and needs no separate label, it is sometimes referred to as "professional negligence."[36]

Unfortunately, "professional negligence" also has become a shorthand term among lawyers and judges for the violation of the architect's implied contractual standard of care. Similarly, courts often refer to "negligent breach of contract" in discussing duties

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perfection of his work."); Donnelly Constr. Co. v. Oberg/Hunt/Gilleland, 139 Ariz. 184, ___, 677 P.2d 1292, 1297 (1984) ("Design professionals, in the absence of an express guarantee, do not 'warrant' that their work will be 'accurate' . . . . [T]hey 'warrant' merely that they have exercised their skills with care and diligence and in a reasonable, non-negligent manner."); Bayshore Dev. Co. v. Bonfoey, 75 Fla. 455, ___, 78 So. 507, 509 (1918); Coombs v. Beede, 89 Me. 187, ___, 36 A. 104, 105 (1896) ("The undertaking of an architect implies that he possesses skill and ability, including taste, sufficient to enable him to perform the required services at least ordinarily and reasonably well; and that he will exercise and apply, in the given case, his skill and ability, his judgment and taste, reasonably and without neglect. But the undertaking does not imply or warrant a satisfactory result."); Chapel v. Clark, 117 Mich. 638, ___, 76 N.W. 62, 62 (1898); Wills v. Black & West, Architects, 344 P.2d 581, 584 (Okla. 1959); Bloomsburg Mills, Inc. v. Sordoni Constr. Co., 401 Pa. 358, ___, 164 A.2d 201, 203 (1960); Ryan v. Morgan Spear Assocs., 546 S.W.2d 678, 681 (Tex. Civ. App. 1977). *See also* Annotation, *Responsibility of One Acting as Architect for Defects or Insufficiency of Work Attributable to Plans*, 25 A.L.R.2d 1085 (1952).

33. *Surf Realty*, 195 Va. at 443, 78 S.E.2d at 908.

34. *Id.*

35. RESTATEMENT (SECOND) OF TORTS § 324A (1965).

36. *See* Annotation, *Necessity of Expert Testimony to Show Malpractice of Architect*, 3 A.L.R. 4th 1023 (1981) and cases cited therein.

owed to the general public on account of the defendant's potential for causing physical harm.[37] Such imprecise terms may seem free of vice until one recognizes that they tend to pull tort logic into the arena of commercial transactions where policy considerations are quite different. As noted in Part I, the public policy behind the law of negligence is to prevent or redress personal injury, while in contract cases such as *Surf Realty* the goal is to give the parties the benefit of their bargain. However, some courts have failed to recognize the fundamental difference between tort and contract causes of action. Predictably, this analysis has led to an explosion of contract disputes tried under tort rules.

III. Development of the Doctrine Permitting Actions in Negligence for Purely Economic Loss

A. *The Decline of the Privity Doctrine*

The distinction between the negligence and contract theories of recovery began to blur in the first half of the twentieth century with the development of products liability law. Until Judge Cardozo's opinion in *MacPherson v. Buick Motor Co.*,[38] the absence of a contractual relationship between a consumer and manufacturer usually was a bar to any recovery.[39] Manufacturers were subject to a socially imposed duty of care only to those with whom they had privity. Thus, consumers of products delivered through the normal distribution network of middlemen and retailers had no direct recourse against the manufacturer for product-related injuries.

In *MacPherson*, the plaintiff purchased a Buick automobile from a dealer. A wheel on the car collapsed and the plaintiff was injured. The plaintiff filed a negligence action against Buick and obtained a judgment. The New York Court of Appeals, through Judge Cardozo, rejected Buick's argument that the lack of privity between it and the plaintiff precluded recovery and affirmed the judgment.

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37. For example, in Keel v. Titan Construction Corp., a case involving only economic loss case, the Oklahoma Supreme Court stated that "[a]ccompanying every contract is a common-law duty to perform it with care, skill, reasonable experience and faithfulness the thing agreed to be done, and a negligent failure to observe any of these conditions is a tort, as well as a breach of contract." 639 P.2d 1228, 1232 (Okla. 1981); *see also* United States v. Rogers & Rogers, 161 F. Supp. 132, 135 (S.D. Cal. 1958).

38. 217 N.Y. 382, 111 N.E. 1050 (1916).

39. *See* W. Prosser & W. Keeton, *supra* note 1, § 96 at 683. There were exceptions to the rule of nonliability, such as for injuries caused by inherently dangerous products. Judge Cardozo's opinion reviews several cases applying the exceptions. *MacPherson*, 217 N.Y. at ___, 111 N.E. at 1051-52.

The court ruled that where a product is "reasonably certain to put life and limb in peril" and will probably be used by persons other than the purchaser, a manufacturer owes a duty imposed by law to use reasonable care to prevent the potential harm.[40] The court dismissed the notion that a manufacturer's duty grows out of his contract alone. According to the court, it "put the source of the obligation where it ought to be . . . in the law."[41]

Not surprisingly, Judge Cardozo did not discuss the distinction between physical damage and purely economic losses. The case before him involved personal injuries and, therefore, was appropriate for tort analysis. Throughout the opinion it is clear that the reason for imposing a duty was the potential for injury to person or property.[42]

By 1966, the rule established in *MacPherson* had been adopted throughout the United States. In products cases, § 2-318 of the UCC has all but eliminated the privity defense:

> Lack of privity between plaintiff and defendant shall be no defense in any action brought against the manufacturer or seller of goods to recover damages for breach of warranty express or implied, or for negligence, although the plaintiff did not purchase the goods from the defendant, if the plaintiff was a person whom the manufacturer or seller might reasonably have expected to use, consume or be affected by the goods . . . .[43]

In addition, a series of judicial decisions and statutes has virtually eliminated the privity defense in other tort cases.[44] The decline of privity doctrine in products liability cases was an extension of the same social policy underpinning negligence law; the reallocation of

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40. *MacPherson*, 217 N.Y. at ___, 111 N.E. at 1053.

41. *Id.*

42. For example, Judge Cardozo quoted excerpts from Heaven v. Pender, 11 Q.B.D. 50 (1883), repeatedly emphasizing the concern for the " 'danger to their person or property' " 217 N.Y. at ___, 111 N.E. at 1052-53. Also, the cases cited in support of the decision involved personal injuries. *Id.* at ___, 111 N.E. at 1051-52.

43. VA. CODE ANN. § 8.2-318 (Added Vol. 1965).

44. W. PROSSER & W. KEETON, *supra* note 1, § 96, at 683. Virginia's general anti-privity statute provides that "[i]n cases not provided for in § 8.2-318 [Section 2-318 of the U.C.C.] where recovery of damages for injury to person, including death, or to property resulting from the negligence is sought, lack of privity between the parties shall be no defense." VA. CODE ANN. § 8.01-223 (Repl. Vol. 1984). *But see* Gravely v. Providence Partnership, 549 F.2d 958, 960 (4th Cir. 1977) (Section 8.01-223 does not alter the rule requiring privity of contract in warranty actions against architects).

risk from injured party to responsible party.[45]

Eventually, the rule of *MacPherson* found its way to the construction industry. The rule was first applied in the construction context by the New York Court of Appeals in *Inman v. Binghamton Housing Authority*.[46] In *Inman*, a child was injured in a fall from the porch of an apartment building and an action was brought against the architect who had designed the project. In overruling the architect's privity defense, the court followed *MacPherson*, indicating that there was no meaningful distinction between injuries caused by chattels (such as the automobile in *MacPherson*) and those involving structures built upon the land.[47] Courts and legislatures throughout the country have followed New York's lead in eliminating the privity defense in personal injury claims relating to buildings.[48]

B. *Tort Actions for Purely Economic Loss*

Both *MacPherson v. Buick Motor Co.* and *Inman v. Binghamton Housing Authority* involved personal injuries. As noted in Part I, negligence law has developed to compensate personal injury victims. Thus, elimination of the privity defense and the application of negligence principles with respect to such injuries is consistent with tort principles. However, tort law is not designed to provide relief to those who have suffered purely economic losses. Certainly Judge Cardozo did not anticipate that the law of negligence would be extended to cases involving purely economic losses. As mentioned above, the fundamental concern expressed in *MacPherson* was the threat of personal injuries and physical damage to property posed by defective automobiles.

Nevertheless, it was probably inevitable that aggrieved parties and enterprising attorneys would attempt to apply the logic of the "anti-privity" cases to disputes involving economic losses. The ar-

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45. For a thorough but relatively brief review of the development of United States products liability law in the twentieth century, see W. PROSSER & W. KEETON, *supra* note 1, §§ 95-98.

46. 3 N.Y.2d 137, 143 N.E.2d 895, 164 N.Y.S.2d 699 (1957).

47. *Id.* at 144, 143 N.E.2d at 898-99, 164 N.Y.S.2d at 703. After rejecting the architect's privity defense, the court ruled that the plaintiff's complaint should be dismissed because it did not allege a latent defect in the porch. *Id.* at 145-46, 143 N.E.2d at 899-900, 164 N.Y.S.2d at 705.

48. *See* Note, *The Crumbling Tower of Architectural Immunity: Evolution and Expansion of Liability to Third Parties*, 45 OHIO ST. L.J. 217, 219-22 (1984).

gument is that since privity is no longer required to maintain a tort action, any "negligent" breach of contract may support a tort action by any affected party. Regrettably, many courts have been receptive to this reasoning. A typical example is the Florida Supreme Court decision in *A. R. Moyer, Inc. v. Graham.*[49]

In *Moyer*, a general contractor asserted in federal court a negligence claim against an architect seeking to recover economic damages (presumably costs related to delay and interference). The United States Court of Appeals for the Fifth Circuit certified a series of questions of law to the Florida court, including the following: "may a general contractor maintain a direct action against the supervising Architect . . . for the general contractor's damages proximately caused by the *negligence* of the Architect . . . where there is an absence of direct privity of contract between the parties."[50] How could any fair-minded judge answer this question in the negative, especially in light of *MacPherson* and *Inman*?

The *Moyer* court began its analysis by discussing the "privity" concept. The court stated that "[p]rivity is a theoretical device of the common law that recognizes limitation of liability commensurate with compensation for contractual acceptance of risk. The sharpness of its contours blurs when brought into contact with modern concepts of tort liability."[51] The court promptly dispensed with the lack of privity argument, concluding that foreseeability and proximate cause provided the necessary foundation for extending liability notwithstanding the absence of privity.[52] The court adopted the reasoning of an earlier "anti-privity" case[53] that, since the supervising architect wielded altogether too much control over the contractor, a consequent duty arose on the part of the architect

> to perform without negligence his functions as they affect the contractor. The power of the architect to stop the work alone is tantamount to a power of economic life or death over the contractor. It is only just that such authority, exercised in such a relationship, carry commensurate legal responsibility.[54]

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49. 285 So. 2d 397 (Fla. 1973).

50. 285 So. 2d at 398 (emphasis added).

51. 285 So. 2d at 399.

52. 285 So. 2d at 402.

53. United States v. Rogers & Rogers, 161 F. Supp. 132 (S.D. Cal. 1958) (The court held that a general contractor could assert a claim against the project architect for negligent breach of his duty to approve concrete for the job; the contractor sought damages relating to delays and corrective work.).

54. 285 So. 2d at 401 (quoting United States v. Rogers & Rogers, 161 F. Supp. at 136).

The *Moyer* court did not discuss the basic contract law policy of giving to the contractor the benefit of his bargain and no more,[55] nor did the court discuss the specifics of the builder's agreement. What did the builder's contract say about owner-caused delays? Did the contract include a "no damage for delay clause"?[56] Were liquidated damages provided for? Was there a *force majure* clause triggered by problems with the plans or the architect's performance of his duties? Was the contractor entitled to extra compensation from the owner for the problems it experienced, and if so, on what basis? The court did not address any of these questions. One can imagine that the reason that the contractor decided to assert a tort claim against the architect was to circumvent a provision limiting damages or establishing prerequisites to recovery.[57]

The *Moyer* court answered the Fifth Circuit's questions in a vacuum. It did not have the opportunity to examine the architect's contract with the owner and therefore the court had no way of knowing the nature of the architect's contractual duties.[58] Instead, the court based its decision on what it perceived to be an architect's general duty to protect the economic interests of the participants in a construction project. But architects have no such general duty. With respect to economic interests, their duties vary from project to project and are only those defined in their contracts.

The questions certified on appeal in *Moyer* demonstrate the problem inherent in the metamorphosis of contract claims into tort claims. Presumably, the Fifth Circuit's questions came directly from the contractor's complaint, the trial court having granted a motion to dismiss for failure to state a claim. One question was

55. *See, e.g.*, Orebaugh v. Antonious, 190 Va. 829, 834, 58 S.E.2d 873, 875 (1950) ("A plaintiff is not allowed to recover for a breach of contract more than the actual loss sustained by him, nor is he allowed to be put in a better position than he would have been had the wrong not been done . . . .").

56. A "no damage for delay" clause was at issue in Algernon Blair, Inc. v. Norfolk Redevelopment and Housing Auth., 200 Va. 815, 108 S.E.2d 259 (1959); *see also* Kalisch-Jarcho, Inc. v. City of New York, 58 N.Y.2d 377, 448 N.E.2d 413, 461 N.Y.S.2d 746 (1983).

57. Construction contracts often include notice of claim requirements and other prerequisites to recovering damages from the owner. *See, e.g.*, Blankenship Constr. Co. v. North Carolina State Highway Comm'n, 28 N.C. App. 593, 222 S.E.2d 452 (1976).

58. The Court noted that the architect-owner contract was not included in the record. *Moyer*, 285 So. 2d at 402.

whether the architect was "negligent in failing and refusing to provide the general contractor with final acceptance of the building project in the form of an Architect's Certificate upon the completion of the building."[59] No socially imposed duty exists with respect to the issuance of certificates of completion by architects. Such a duty either arises or does not arise depending upon the terms of the owner-architect agreement. The architect either complies or does not comply with the relevant contract language; in this endeavor his level of performance is not a societal concern and, therefore, is not a tort issue.

Another of the certified questions is similarly flawed because it assumes that the architect "negligently exercised control and supervision over the general contractor."[60] Contract administration duties of architects are set out in their contracts and vary from no duties to full-time on-site representation. The parties are free to decide what contract administration duties, if any, the architect will perform. Thus, there is no societal interest in having architects provide a particular level of administrative duties. In fact, in recent years, owners have turned frequently to "construction managers" as opposed to project architects for contract administration services.

The *Moyer* court assumed that the architect had the right to stop the contractor's work or at least was persuaded by an earlier decision that such a right existed.[61] Again, it is impossible to make such a blanket assumption about contracts for architectural services. Under the terms of the 1963 edition of the General Conditions of the Contract for the Construction of Buildings, published by the American Institute of Architects, the architect had "authority to stop the work whenever such stoppage may be necessary in his reasonable opinion to insure the proper execution of the contract."[62] However, the AIA General Conditions were revised in 1967, and the right to stop work was eliminated. Thus, the *Moyer* court's assumption would have been incorrect if the 1967 form had been used. Moreover, although the AIA forms are in frequent use in the construction industry, they are by no means exclusive. Other construction industry organizations such as the Associated General

59. *Id.* at 398.

60. *Id.*

61. *Id.* at 401 (quoting United States v. Rogers & Rogers, 161 F. Supp. 132 (S.D. Cal. 1958)).

62. American Institute of Architects Document A201 (1963).

Contractors publish form contracts, and government agencies have their own forms which define the duties of the parties according to their special needs. Contrary to the *Moyer* court's apparent assumption, there is no uniform set of architectural duties.

The critical point overlooked by the *Moyer* court is that parties in construction projects define their obligations in their contracts. The duties imposed upon the architect arise from and are limited by his contract and the contractor's rights arise from and are defined by his contract. By trying to decide what level of services the architect should reasonably have provided, the *Moyer* court, in effect, created a new owner/architect contract. This sort of tampering with commercial contracts is unnecessary and unwise. The parties are best situated to determine their needs and negotiate their contract terms accordingly.[63]

The *Moyer* court also ignored the historical difference between economic losses on the one hand and physical damage and personal injuries on the other hand. Two of the three Florida cases relied upon by the court in *Moyer* involved personal injuries[64] and the third involved damage to property resulting from the failure of some roof trusses.[65] After citing these cases with approval and distinguishing Florida decisions denying a tort cause of action to third parties who sustained economic loss as the result of the professional malpractice of a title abstractor[66] and an accountant,[67] the court adopted the reasoning of the California Supreme Court in *Biakanja v. Irving*:[68]

> The determination whether in a specific case the defendant will be held liable to a third person not in privity is a matter of policy and involves the balancing of various factors, among which are the ex-

63. In considering whether punitive damages should be available for contract breaches, the Virginia Supreme Court recently emphasized that contract damages "are within the contemplation and control of the parties in framing their agreement." Kamlar Corp. v. Haley, 224 Va. 699, 706, 299 S.E.2d 514, 517 (1983).

64. Geer v. Bennett, 237 So. 2d 311 (Fla. Dist. Ct. App. 1970) (claim by masonry worker against architect for personal injuries) and Mai Kai, Inc. v. Colucci, 205 So. 2d 291 (Fla. 1967) (claim by restaurant customer against architect for personal injuries caused by falling ceiling fan).

65. Audlane Lumber & Builders Supply, Inc. v. D.E. Britt Assocs., 168 So. 2d 333 (Fla. Dist. Ct. App. 1964) (architect may be liable in tort for foreseeable economic losses despite lack of privity).

66. Sickler v. Indian River Abstract & Guar. Co., 142 Fla. 528, 195 So. 195 (1940).

67. Investment Corp. of Fla. v. Buchman, 208 So. 2d 291 (Fla. App. 1968).

68. 49 Cal. 2d 647, 320 P.2d 16 (1958) (this is the same rationale relied upon in United States v. Rogers & Rogers, 161 F. Supp. 132 (S.D. Cal. 1958)).

> tent to which the transaction was intended to affect the plaintiff, the foreseeability of harm to him, the degree of certainty that the plaintiff suffered injury, the closeness of the connection between the defendant's conduct and the injury suffered, the moral blame attached to the defendant's conduct, and the policy of preventing future harm.[69]

Biakanja involved the unauthorized practice of law by a notary who had drafted a will which was ultimately set aside because of deficiencies in its execution. The California court noted that the notary's action constituted a misdemeanor.[70]

The *Moyer* court did not discuss the different policy considerations underlying tort and contract law, the rules of damages appropriate to each, the application of contract requirements and conditions, or the means by which these new tort duties would be coordinated with the contractual structure at the time of trial. Instead, without adequately considering the consequences, the court simply extended the "anti-privity" rationale from the physical injury area to cases involving purely economic losses.

The Fifth Circuit also asked the *Moyer* court whether, under Florida law, the general contractor was a third party beneficiary of the contract between the owner and the architect. With admirable brevity, the court answered in the negative, concluding that "supervision generally is undertaken for the benefit of the owner to insure that the construction is proceeding in compliance with the plans and specifications approved by the owner."[71] In other words, the court held that although the architect owed a contractual duty to the owner with regard to supervision, he did not owe the duty to the general contractor.

The *Moyer* court's two rulings seem inconsistent. The court found a tort duty with respect to economic losses while simultaneously concluding that the architect's duties to supervise were not intended to benefit the contractor. However, the first required element of a cause of action in negligence is the existence of a duty owed to the plaintiff by the defendant. Where did the tort duty

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69. 49 Cal. 2d at ___, 320 P.2d at 19.

70. *Id.*

71. 285 So. 2d at 403. Most courts that have considered the issue are in accord. *See, e.g.*, Valley Landscape Co. v. Rolland, 218 Va. 257, 262-63, 237 S.E.2d 120, 124 (1977) (contractor is not a third-party beneficiary of landscape architect's contract with the owner where no facts indicate that the contract was "clearly and definitely intended" to benefit the contractor).

arise from if not from the contract? This inconsistency is magnified when one considers that, as the Virginia Supreme Court has pointed out, an "owner employs an architect, to a degree, to protect himself from the contractor."[72]

In a dissenting opinion in *Moyer*, Justice Dekle summarized several of the problems with the majority opinion:

> The liability of the architect should follow logical and mutually agreed or reasonably implied lines of responsibility between contractor and architect, within which framework an architect's failures can then be asserted in a proper claim. Moreover, such claims can, of course, be pursued by the owner against the architect where the contractor has successfully asserted the claim or defense against the owner. Bonds are also traditionally provided for such contingencies. Neglect to agree in advance on responsibilities or to take available precautions should not be the basis for corrupting established and well founded principles of liability.[73]

Justice Dekle could have added that the majority's focus on the privity issue was inappropriate. The elimination of the privity requirement did not create new theories of recovery; it merely eliminated a historical defense. The real question, which the *Moyer* court addressed secondarily and without the benefit of the contract at issue, is whether the duty alleged exists.

C. *The Extension of the* Moyer *Doctrine*

The *Moyer* Doctrine has been adopted in at least seven states. The states apparently in the *Moyer* camp are: Alabama, Arizona, California, Louisiana, Mississippi, North Carolina, and Washington.[74] Courts in at least eight states, Alaska, Illinois, Indiana, Iowa, Kentucky, Minnesota, Texas, and Virginia, have expressed the opposite view.[75]

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72. *Valley Landscape Co.*, 218 Va. at 261, 237 S.E.2d at 123.

73. 285 So. 2d at 404 (Deckle, J., concurring in part and dissenting in part).

74. Owen v. Dodd, 431 F. Supp. 1239 (N.D. Miss. 1977); United States v. Rogers & Rogers, 161 F. Supp. 132 (S.D. Cal. 1958); Berkel & Co. Contractors, Inc. v. Providence Hosp., 454 So. 2d 496 (Ala. 1984); Donnelly Constr. Co. v. Oberg/Hunt/Gilleland, 677 P.2d 1292 (Ariz. 1984); Gurtler, Hebert & Co. v. Weyland Machine Shop, Inc., 405 So. 2d 660 (La. Ct. App. 1981); Quail Hollow East Condominium Assoc. v. Donald J. Scholz Co., 47 N.C. App. 518, 268 S.E.2d 12 (1980). *But see* Detweiler Bros. v. John Graham & Co., 412 F. Supp. 416 (E.D. Wash. 1976); McKinney Drilling Co. v. Nello L. Teer Co., 38 N.C. App. 472, 248 S.E.2d 446 (1978).

75. State *ex rel.* Smith v. Tyonek Timber, Inc., 680 P.2d 1148 (Alaska 1984); Anderson

Conforti & Eisele, Inc. v. John C. Morris Associates,[76] is typical of the opinions supporting the *Moyer* view. In *Conforti*, the trial court considered the defendant engineer's motion to dismiss the plaintiff contractor's complaint for failure to state a claim. As in *Moyer*, the trial judge began his analysis with the privity issue. The issue as posed by the court was whether a design professional was answerable in tort to a contractor who sustains economic damages as a result of the negligence of the design professional in the absence of privity of contract. The court noted that the privity defense was not favored in New Jersey, and that it had been abrogated in cases involving personal injuries caused by the negligence of design professionals.[77]

> Is there a valid reason why the negligence principles adopted in the *Totten* and *Schipper* cases [involving personal injuries] should not be applied here? Should recovery be denied to an innocent contractor who likewise suffers injuries, albeit economic damage, as a result of the negligence of the design professional? I think the answer to both questions is no.[78]

The *Moyer* Doctrine has been accepted by some courts as a logical extension of the authorities permitting recovery for personal in-

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Elec. Inc. v. Ledbetter Erection Corp., 133 Ill. App. 3d 844, 479 N.E.2d 476 (1985), *aff'd*, 115 Ill. 2d 146, 503 N.E.2d 246 (1986). *But see* Case Prestressing Corp. v. Chicago College of Osteopathic Medicine, 118 Ill. App. 3d 782, 455 N.E.2d 811 (1983); Peyronnin Constr. Co. v. Weiss, 137 Ind. App. 417, 208 N.E.2d 489 (1965); Blake Constr. Co. v. Alley, ___ Va. ___, 353 S.E.2d 724 (1987). *But cf.* Bryant Elec. Co. v. City of Fredericksburg, 762 F.2d 1192 (4th Cir. 1985); Essex v. Ryan, 446 N.E.2d 368 (Ind. Ct. App. 1983); Nebraska Innkeepers, Inc. v. Pittsburgh-Des Moines Corp., 345 N.W.2d 124 (Iowa 1984); Penco, Inc. v. Detrex Chem. Indus., Inc., 672 S.W.2d 948 (Ky. Ct. App. 1984); D&A Dev. Co. v. Butler, 357 N.W.2d 156 (Minn. App. 1984); Bernard Johnson, Inc. v. Continental Constructors, Inc., 630 S.W.2d 365 (Tex. Ct. App. 1982).

76. 175 N.J. Super. 341, 418 A.2d 1290 (1980). The Supreme Court of New Jersey has not decided whether purely economic losses arising out of a construction project are recoverable in negligence. The court specifically refrained from ruling on the issue in Aronsohn v. Mandara, 98 N.J. 92, ___, 484 A.2d 675, 683 (1984) (holding that a subsequent buyer of a house may recover economic damages on implied warranty theory from builder), and ruled in Spring Motors Distribs. Inc. v. Ford Motor Co., 98 N.J. 555, ___, 489 A.2d 660, 672-74 (1985) that economic damages are not available under negligence or strict liability theories in the product liability context. *See also* New Mea Constr. Corp. v. Harper, 203 N.J. Super. 486, 497 A.2d 534, 538-41 (1985) (holding that an owner may not recover in negligence against a construction supervisor for purely economic losses). In light of these decisions, New Jersey is not listed among the states that have taken a position on the "economic loss" issue.

77. 175 N.J. Super. at ___, 418 A.2d at 1291 (citing Totten v. Gruzen, 52 N.J. 202, 245 A.2d 1 (1968) and Schipper v. Levitt & Sons, 44 N.J. 70, 207 A.2d 314 (1965)).

78. *Id.* at ___, 418 A.2d at 1292.

juries suffered as the result of the breach of contractually assumed duties. As in *Moyer* itself, the focus has been upon the acknowledged ill-health of the privity doctrine, and not upon the basic policy issues involved. The decisions do not discuss the relationship between the general contractor and the owner. They do not consider that an agency relationship exists between the owner and the architect; nor do they take account of the policy differences between tort law and commercial contract law and the different application of those policies to economic loss as opposed to physical damage.

IV. THE EMERGENCE OF THE "ECONOMIC LOSS" RULE IN PRODUCTS LIABILITY CASES

While some participants in the construction industry have been attempting to extend the application of tort principles, products liability plaintiffs have been undertaking a similar effort. Commercial products liability plaintiffs have attempted to recover purely economic losses from manufacturers with whom they are not in privity. Similarly, they have attempted to apply negligence or strict liability principles even where they have the right to pursue a contract action against the manufacturer.

For more than two decades courts and commentators have debated whether negligence and strict liability principles, as opposed to contract rules, should be applied in products cases involving purely economic damages.[79] Like their counterparts in the construction field, many of the courts considering the issue have focused on the privity doctrine and have not adequately considered the underlying policy issues.[80] Recently, however, several courts have analyzed the basic policy issues and have concluded that negligence principles are not compatible with economic loss claims.

The Illinois Supreme Court's recent decision in *Moorman Manufacturing Co. v. National Tank Co.*,[81] denied a negligence claim brought to recover purely economic losses. Moorman purchased a grain-storage tank from National Tank. A crack eventually devel-

79. *See, e.g.*, Note, *Economic Loss in Products Liability Jurisprudence*, 66 COLUM. L. REV. 917 (1966); Comment, *Manufacturers' Liability to Remote Purchasers for "Economic Loss" Damages—Tort or Contract?*, 114 U. PA. L. REV. 539 (1966).

80. *See, e.g.*, Berg v. General Motors Corp., 87 Wash. 2d 584, 555 P.2d 818 (1976) (commercial fisherman allowed to assert a negligence claim for lost profits against manufacturer and seller of boat engine and clutch).

81. 91 Ill. 2d 69, 435 N.E.2d 443 (1982).

oped in the tank and Moorman asserted strict liability, negligence and warranty claims against National Tank. Moorman sought to recover the cost of repairing the crack and damages for the loss of use of the tank.[82]

The question before the Illinois court was whether Moorman could recover its economic losses under strict liability and negligence theories. There was no lack of privity because Moorman had purchased the tank directly from National Tank. In a unanimous decision, the court ruled that purely economic losses could not be recovered under either strict liability or negligence theories.[83]

After reviewing the seminal *Santor v. A & M Karagheusian, Inc.*[84] and *Seely v. White Motor Co.*[85] cases, the *Moorman* court considered the basic purposes of contract and tort law. Products liability tort law, the court observed, provides compensation for physical injury caused by unreasonably dangerous products, while contract law protects expectation interests.[86] The court also noted that "the law of sales has been carefully articulated to govern suppliers and consumers of goods."[87] Among other problems, allowing tort recovery for economic losses in products cases would take away a manufacturer's UCC section 2-316 right to limit or eliminate warranties.[88]

The court concluded that it was unnecessary to apply "the safety-insurance policy of tort law" to protect commercial expectations where there is no personal injury or physical damage other than to the product itself, and that the "remedy for economic loss, loss relating to a purchaser's disappointed expectations due to deteriorating internal breakdown or nonaccidental cause . . . lies in contract."[89] The court stated that "[a]llowing an aggrieved party to recover under a negligence theory for solely economic loss would

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82. *Id.* at ___, 435 N.E.2d at 445.

83. *Id.* at ___, 435 N.E.2d at 450-51.

84. 44 N.J. 52, 207 A.2d 305 (1965) (strict liability in tort claim against manufacturer allowed for loss of value of carpeting).

85. 63 Cal. 2d 9, 403 P.2d 145, 45 Cal. Rptr. 17 (1965) (economic losses not recoverable under strict liability theory absent personal injury or physical damage to property).

86. 91 Ill. 2d at ___, 435 N.E. 2d at 448.

87. *Id.* at ___, 435 N.E.2d at 447.

88. *Id.* Section 2-316 of the UCC permits sellers to exclude the implied warranties of merchantability and fitness for a particular purpose and sets forth requirements for warranty exclusions. Section 2-719 permits contractual modification of the normal UCC remedies in some circumstances.

89. 91 Ill. 2d at ___, 435 N.E.2d at 450.

constitute an unwarranted infringement upon the scheme provided by the UCC."[90]

The *Moorman* decision left open at least two possible avenues of tort relief for purely economic loss in commercial cases. First, the court stated that economic loss caused by intentional misrepresentations is recoverable in tort.[91] Second, the court reaffirmed its earlier ruling in *Rozny v. Marnul* that economic losses are recoverable "where one who is in the business of supplying information for the guidance of others in their business transactions makes negligent misrepresentations."[92] If not applied judiciously, the *Rozny* negligent misrepresentation exception could eviscerate the economic loss rule established in *Moorman*. For example, mistakes in design professionals' plans or specifications could easily become "negligent misrepresentations" allowing contractors to circumvent their contracts.[93]

The New Jersey Supreme Court, in *Spring Motor Distributors, Inc. v. Ford Motor Co.*,[94] also ruled that a commercial buyer may not recover purely economic losses under negligence or strict liability theories. In this case, the plaintiff purchased a fleet of trucks

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90. *Id.* at ___, 435 N.E.2d at 452.

91. *Id.*

92. *Id. See infra* note 93; *see also* Horsell Graphic Indus. v. Valuation Counselors, Inc., 639 F. Supp. 1117, 1121 (N.D. Ill. 1986) (apparently applying the negligent misrepresentation exception holding that the *Moorman* decision did not apply to a suit against an appraisal firm for breach of contract and negligence in the issuance of a stock valuation report).

93. In Rozny v. Marnul, 43 Ill. 2d 54, 250 N.E.2d 656 (1969). In *Rozny*, a homeowner sued a surveyor, with whom he had no contract, for damages caused by a negligent survey. The court, focusing on the privity doctrine rather than the policy issues underlying the doctrine, held that the plaintiffs could recover their damages (the cost of moving and then repairing the plaintiff's house and garage) from the surveyor. 43 Ill. 2d at ___, 250 N.E.2d at 663. The court stated that six factors were relevant to its holding:

> (1) The express, unrestricted and wholly voluntary "absolute guarantee for accuracy" appearing on the face of the inaccurate plat;
> (2) Defendant's knowledge that this plat would be used and relied on by others than the person ordering it, including plaintiffs;
> (3) The fact that potential liability in this case is restricted to a comparatively small group, and that, ordinarily, only one member of that group will suffer loss;
> (4) The absence of proof that copies of the corrected plat were delivered to anyone;
> (5) The undesirability of requiring an innocent reliant party to carry the burden of a surveyor's professional mistakes;
> (6) That recovery here by a reliant user whose ultimate use was foreseeable will promote cautionary techniques among surveyors.

Id. The *Rozny* opinion does not discuss why the plaintiffs did not seek to recover from the party from whom they purchased the property.

94. 98 N.J. 555, 489 A.2d 660 (1985).

from a Ford dealer. Soon after delivery, the trucks developed severe problems with their transmissions and the buyer sued Ford, the dealer, and the manufacturer of the transmissions for decreased market value of the trucks and consequential damages (*e.g.* lost profits and towing costs).[95] The buyer asserted UCC warranty, negligence, and strict liability claims against each defendant. The trial court ruled that the tort theories were inapplicable and that the case should be dismissed because it was filed after the expiration of the four-year UCC statute of limitations. The New Jersey intermediate appellate court reversed, holding that the buyer stated a cause of action for strict liability in tort and therefore the six-year tort limitation period was applicable.[96]

The New Jersey Supreme Court reversed. As did the Illinois court in *Moorman*, the court focused on both the nature of the transaction and the type of loss suffered. According to the court, the truck purchase was an ordinary commercial transaction between parties with "substantially equal bargaining positions."[97] The court observed that the UCC was designed for just such transactions[98] and emphasized that tort theories of recovery were developed to protect society's general interest in freedom from physical harm rather than freedom from economic losses.[99] As the court stated, "a seller's [tort] duty of care generally stops short of creating a right in a commercial buyer to recover purely economic loss."[100]

The New Jersey Supreme Court's opinion in *Spring Motor Distributors* contrasts sharply with the decision of the New Jersey Superior Court in *Conforti*.[101] The distinction is that the *Conforti* court focused on the privity issue, while in *Spring Motor Distributors* the Supreme Court focused its analysis on the purposes of contract and tort law.

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95. *Id.* at ___, 489 A.2d at 664.

96. *Id.* at ___, 489 A.2d at 664-65. *Spring Motor Distributors* illustrates one reason why plaintiffs try to extend the boundaries of tort law: sometimes contract claims (but not tort claims) are barred by the applicable statutes of limitation. However, if the limitation periods are unfair or cause confusion, the solution is to change limitation rules. Courts should not try to solve the problem by ignoring the very real differences between tort and contract theories of recovery.

97. *Id.* at ___, 489 A.2d at 671.

98. *Id.*

99. *Id.* at ___, 489 A.2d at 672. The court ruled that the buyer could assert UCC warranty claims against the transmission supplier despite a complete lack of privity. *Id.* at ___, 489 A.2d at 677. This is a departure from the general rule.

100. *Id.* at ___, 489 A.2d at 672.

101. *See supra* notes 76-77 and accompanying text.

V. THE ECONOMIC LOSS RULE IN CONSTRUCTION INDUSTRY CASES: AN EMERGING TREND

A few months after deciding *Moorman Manufacturing Co. v. National Tank Co.*, the Illinois Supreme Court applied the economic loss rule in a construction industry case. In *Redarowicz v. Ohlendorf*,[102] the court ruled that the second owner of a home could not recover economic losses (the cost of repairing structural defects) from the builder under a negligence theory.[103] Elaborating on its ruling in *Moorman*, the court stated that:

> [t]his is not a case where defective construction created a hazard that resulted in a member of the plaintiff's family being struck by a falling brick from the chimney. The adjoining wall has not collapsed on and destroyed the plaintiff's living room furniture. The plaintiff is seeking damages for the costs of replacement and repair of the defective chimney, adjoining wall and patio. While the commercial expectations of this buyer have not been met by the builder, the only danger to the plaintiff is that he would be forced to incur additional expenses for living conditions that were less than what was bargained for. The complained-of economic losses are not recoverable under a negligence theory.[104]

While rejecting the plaintiff's negligence claim, the court extended Illinois' implied warranty of habitability to cover subsequent purchasers of residential dwellings.[105] The plaintiff was allowed to proceed against the builder on the implied warranty theory, prompting some critics, including Chief Justice Ryan in his dissent, to suggest that the *Moorman* economic loss rule was already dead.[106] However, the real value of the economic loss rule is that it assures that commercial law will be applied to commercial contracts. Creating a direct warranty cause of action between an individual home buyer and a builder may be viewed as a consumer law exception to the rule rather than as a rejection of it. Indeed, subsequent Illinois decisions indicate that the economic loss rule applied in *Moorman* is still alive and that the Illinois Supreme

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102. 92 Ill. 2d 171, 441 N.E.2d 324 (1982).
103. *Id.* at ___, 441 N.E.2d at 326-27.
104. *Id.* at ___, 441 N.E.2d at 327.
105. *Id.* at ___, 441 N.E.2d at 330-31.
106. *Id.* at ___, 441 N.E.2d at 332 (Ryan, C.J., dissenting).

Court continues to give precedence to contract terms in commercial economic loss cases.[107]

While avoiding the economic loss issue, the Illinois Supreme Court ruled in *Ferentchak v. Village of Frankfort*[108] that an architect's or engineer's duties to third parties are limited by his contractual obligations to his client. In *Ferentchak*, a developer hired an engineer to design a drainage system for a residential subdivision. At the developer's request, the engineer's design did not include minimum foundation grade elevations for the subdivision lots. The engineer's design included a twenty-foot-wide drainage channel but did not provide other specifications for the channel. The plaintiffs purchased a house and lot located next to the drainage channel from a contractor, who had purchased the lot from the developer. Soon after the plaintiffs occupied the house, they noticed water accumulating in their back yard. The water eventually found its way into the plaintiffs' basement. The plaintiffs filed a negligence claim against the developer, the engineer, the contractor, and the village in which the house was located. The trial court granted summary judgment for the developer and the jury found that the contractor had not been negligent. The jury determined that the engineer and town had been negligent and these defendants appealed.

On appeal the engineer argued that the economic loss rule of *Moorman* precluded the plaintiffs' recovery against him. The court, however, did not address this argument, perhaps because there was water damage to property other than the house itself. Instead the court ruled that the engineer was not liable for the plaintiffs' damages because his contract did not impose a duty to provide minimum foundation elevations or specify the dimensions of the drainage channel.[109] The engineer's contract provided that the foundation grade levels were the responsibility of the individual home builders and the developer.[110]

The court's focus on the engineer's duty and his contract is in keeping with the philosophy of *Moorman*. The economic loss rule is simply a shorthand way of determining the duty issue in cases

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107. *See, e.g.*, Ferentchak v. Village of Frankfort, 105 Ill. 2d 474, 475 N.E.2d 822 (1985).

108. 105 Ill. 2d 474, 475 N.E.2d 822 (1985).

109. *Id.* at ___, 475 N.E.2d at 826.

110. *Id.* at ___, 475 N.E.2d at 825. The question raised by *Moorman*, which the court avoided in *Ferentchak*, is: *to whom* is the duty owed? In *Ferentchak* the court focused on whether the engineer owed the duty in question to anyone. *Id.*

involving purely economic damages. In cases involving physical damage or personal injury, the duty question is also paramount. Significantly, the court rejected the notion that the engineer breached his general duty as a professional by failing to provide the information. According to the court "[t]he degree of skill and care required of [the engineer] in this situation is dependent on his contractual obligation."[111]

In the *Ferentchak* opinion, the court did not comment on the intermediate court's ruling that the *Moorman* rule barred tort actions only where the plaintiff had an adequate contractual remedy against the defendant. The intermediate court explained that the purchaser's contract action would be against the builder, "who would then be left to possible third party actions against those responsible in the chain of production."[112] This remedy was, according to the intermediate court, "inadequate, however conceptually sound, and not intended by the Court in *Moorman*."[113] The intermediate court did not explain why the traditional contract remedy was unsatisfactory.

In *Anderson Electric, Inc. v. Ledbetter Erection Corp.*,[114] an Illinois appellate court applied the economic loss rule to bar an electrical subcontractor's claim against a construction supervisor. In *Anderson Electric*, the subcontractor claimed that the construction supervisor, with whom the subcontractor had no direct contractual relationship, breached its duty by

> failing to hold regular job site meetings, by supplying faulty materials, by giving improper directions regarding the performance of [the subcontractor's] work, by failing to properly inspect the work done on an ongoing basis, and by failing to stop the work when it knew or should have known that the work was unacceptable.[115]

The subcontractor claimed that the supervisor's negligence caused it to have to redo portions of its work at a cost of almost $300,000. The opinion contains no hint as to why the subcontractor did not file suit against its contractual partner, the general contractor.

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111. 105 Ill. 2d at ___, 475 N.E.2d at 826. In a personal injury case an engineer could be held to a higher standard than that provided in his contract.

112. 121 Ill. App. 3d. 599, ___, 459 N.E.2d 1085, 1092 (1984).

113. *Id.*

114. 133 Ill. App. 3d 844, 479 N.E.2d 476 (1985).

115. *Id.* at ___, 479 N.E.2d at 477.

The court determined that the subcontractor's claim for the cost of redoing portions of the work was for purely economic loss. The court then applied the rule established in *Moorman* which it stated as follows: "in general, tort actions should be confined to situations involving physical harm or property damage, as distinguished from purely economic loss for which redress should be sought in a contract action."[116] The court rejected the notion introduced by the intermediate court in *Ferentchak* that the economic loss rule barred a tort action only if an alternate cause of action were available against the defendant in question. The court also rejected the statement of another Illinois intermediate appellate court that the *Moorman* rule should not apply if it would leave the plaintiff wholly without a remedy.[117]

Finally, the court rejected the plaintiff's argument that the negligent misrepresentation exception set forth in *Rozny v. Marnul*[118] applied to permit the subcontractor's action against the construction supervisor. This part of the decision indicates that the negligent misrepresentation exception will be applied sparingly. This is a welcome development, since the liberal application of the negligent misrepresentation theory, without due consideration for the fundamental difference between tort and contract duties, could gut the *Moorman* economic loss rule.

The Fourth Circuit Court of Appeals' decision in *Bryant Electric Co. v. City of Fredericksburg*[119] may signal a trend toward the application of the economic loss rule to construction industry disputes outside Illinois. In *Bryant Electric*, the Fourth Circuit held that under Virginia law a contractor may not recover purely economic losses from an engineer based on negligence when the contractor and engineer are not in privity. Judge Sneeden's opinion relies primarily upon Virginia authorities but also cites the economic loss rule in support of the holding.[120]

Bryant Electric arose out of a construction project with standard contractual relationships. Bryant contracted with the City of Fredericksburg to construct an aqueduct and perform related restoration work. The city hired Malcolm Pirnie, Inc., to provide ar-

116. *Id.* at ___, 479 N.E.2d at 478.

117. Bates & Rogers Constr. Corp. v. North Shore Sanitary Dist., 128 Ill. App. 3d 962, 471 N.E.2d 915 (1984).

118. *See supra* note 93.

119. 762 F.2d 1192 (4th Cir. 1985).

120. *Id.* at 1195 n.6.

chitectural and engineering design and contract administration services for the project. The project was typical in that Bryant and Malcolm Pirnie had no contractual relationship.

Bryant filed suit in the United States District Court for the Eastern District of Virginia against both the city and Malcolm Pirnie. The claims against Malcolm Pirnie were based on negligence. In its complaint, Bryant alleged that errors by Malcolm Pirnie in the design and "supervision" of the project caused significant delays in the work and additional expense to Bryant. Bryant sought a joint and several judgment against Malcolm Pirnie and the city. Judge Mehrige ruled that Bryant could not recover economic losses from Malcolm Pirnie,[121] and Bryant appealed.

Since *Bryant Electric* was a diversity claim, Judge Sneeden looked to Virginia case law for controlling authority. Noting that the Supreme Court of Virginia had not ruled on the issue,[122] he reviewed the decisions of circuit courts around the Commonwealth. Judge Sneeden observed that the circuit courts "have consistently held that a contractor may not recover for purely economic losses suffered as a result of an architect's or engineer's negligence absent privity of contract."[123]

The opinion also looked for guidance to the Virginia Supreme Court's opinion in *Ayyildiz v. Kidd*,[124] which held that a doctor who successfully defended a malpractice suit did not have a negligence cause of action against the plaintiff's attorney. Judge Sneeden noted that the Virginia court held that the attorney's duty was to his client alone.[125] In *Ayyildiz*, the Virginia Supreme Court quoted with approval from the Iowa Supreme Court's opinion in *Brody v. Ruby*:[126]

> [a]bsent special circumstances, it generally is held an attorney can be liable for consequences of professional negligence only to a client

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121. *Id.* at 1193. Judge Merhige also sustained the city's Rule 12(b)(6) motion to dismiss Bryant's claim based on a forum selection clause in Bryant's contract requiring that all claims "shall be decided by the Circuit Court of the City of Fredericksburg." 762 F.2d at 1196. The Fourth Circuit affirmed this ruling.

122. *Id.* at 1193. In the interim since *Bryant Electric* was decided by the Fourth Circuit, the Virginia Supreme Court has ruled on the economic loss issue in Blake Construction Co. v. Alley, ___ Va. ___, 353 S.E.2d 724 (1987). *See infra* notes 130-34 and accompanying text.

123. 762 F.2d at 1193.

124. 220 Va. 1080, 266 S.E.2d 108 (1980).

125. 762 F.2d at 1194 n.3.

126. 267 N.W.2d 902 (Iowa 1978).

> . . . . The courts reasons that if liability would be permitted to a third party without regard to privity, the parties to the contract would be deprived of control of their own agreement.[127]

The Fourth Circuit also cited Professor Prosser on the economic loss rule in the products context:

> [W]here there is no accident, and no physical damage, and the only loss is a pecuniary one, through loss of the value or use of the thing sold, or the cost of repairing it, the courts have adhered to the rule . . . that purely economic interests are not entitled to protection against mere negligence, and so have denied the recovery.[128]

Finally, the court rejected the argument that Virginia Code section 8.01-223, which abolished the lack of privity defense in cases involving "injury to person . . . or to property," also applies to economic loss claims.[129]

In its 1987 decision in *Blake Construction Co. v. Alley*,[130] the Supreme Court of Virginia confirmed the Fourth Circuit's reasoning by holding that section 8.01-223 of the Virginia Code "does not eliminate the privity requirement in a negligence action for economic loss alone."[131] The court reasoned that since section 8.01-223 is in derogation of the common law requirement of privity in negligence actions, it must be strictly construed and could not be applied beyond its express limitation to cases involving injuries to person or property.[132]

The court's decision in *Blake Construction*, while focusing on the scope of Virginia's anti-privity statute, also discussed the fun-

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127. 220 Va. at 1086, 266 S.E.2d at 112.

128. 762 F.2d at 1195 n.6 (quoting W. PROSSER, THE LAW OF TORTS 665 (4th ed. 1971)).

129. Va. Code Section 8.01-223 provides: "*Lack of Privity no defense in certain cases.*—In cases not provided for in Section 8.2-318 where recovery of damages for injury to person, including death, or to property resulting from negligence is sought, lack of privity between the parties shall be no defense." The Fourth Circuit observed that "[a] proper reading of the express terms of Section 8.01-223, therefore, would seem to require some *physical* injury to the plaintiff's property before a suit may be maintained in the absence of privity." 762 F.2d at 1195. The court noted that the comparable Mississippi statute specifically included "economic loss." *Id.* at 1195 n.5.

130. ___ Va. ___, 353 S.E.2d 724 (1987).

131. *Id.* at ___, 353 S.E.2d at 726.

132. *Id.* at ___, 353 S.E.2d at 726. The court stated: "[w]e cannot impute to the General Assembly an intent to abrogate by implication the privity requirement in cases where no [injury to person or property] is alleged, thereby allowing negligence actions for solely economic loss." *Id.* at ___, 353 S.E.2d at 726.

damental difference between tort and contract duties. After observing that an architect has no common law duty to protect a contractor from economic loss, the court stated the broad "economic loss" rule that "[t]here can be no actionable negligence where there is no breach of a duty 'to take care for the safety of the person or property of another.' "[133]

This reasoning should preclude negligence claims for purely economic loss even where the parties are in privity. The nature of the loss and, therefore the source of the duty, governs whether a party may assert a tort cause of action. The court noted that while it would not find an implied duty between the architect and the contractor, the parties could provide for such a duty in their contracts:

> The parties involved in a construction project resort to contracts and contract law to protect their economic expectations. Their respective rights and duties are defined by the various contracts they enter. Protection against economic losses caused by another's failure properly to perform is but one provision the contractor may require in striking his bargain. Any duty on the architect in this regard is purely a creature of contract.[134]

Thus, the court left it to the parties to construction contracts to decide how to protect their economic interests.

The circumstances of *Bryant Electric* and *Blake Construction* illustrate why the economic loss rule should be applied in the context of construction contracts. One reason for applying the economic loss rule is to hold parties to their contracts. Bryant's contract with the city provided that the Circuit Court for the City of Fredericksburg would be the only forum available to the parties. If the Fourth Circuit had allowed Bryant to pursue a negligence claim against Malcolm Pirnie, the case would have been tried in United States District Court and Bryant would have avoided the strict forum selection clause in its contract with the city. Similarly, Blake Construction's contract with the owner (the Commonwealth of Virginia) contained a "no damage for delay clause" as well as

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133. *Id.* at ___, 353 S.E.2d at 726 (quoting Bartlett v. Recapping, Inc., 207 Va. 789, 793, 153 S.E.2d 193, 196 (1967), quoting Atlantic Co. v. Morrisette, 198 Va. 332, 333, 94 S.E.2d 220, 221-22 (1956)).

134. *Id.* at ___, 353 S.E.2d at 727. In fact, owners owe contractors an implied duty to provide workable plans. Contractors may recover damages caused by a breach of this duty. *See infra* notes 136-142 and accompanying text.

other potential limitations on damages. By asserting a tort claim, Blake Construction Co. may have hoped to avoid these contract terms.

Bryant Electric also illustrates the availability of contract relief, properly limited by contract terms, in construction disputes. Bryant filed its consequential damages claim against both the city and the city's engineer.[135] The city never argued that it was not responsible for its engineer's actions and such an argument, if made, could not have prevailed. A majority of courts that have considered the issue have held that an owner warrants that the plans and specifications provided by the designer will, if followed, produce a working structure.[136] The seminal case on the subject is *MacKnight Flintic Stone Co. v. Mayor of New York*,[137] in which the court stated that:

> If there was an implied warranty of sufficiency, it was made by the party who prepared the plan and specifications, because they were his work; and, in calling for proposals to produce a specified result by following them, it may fairly be said to have warranted them adequate to produce that result.[138]

Virginia follows the *MacKnight* rule.[139] The corollary of this rule is that a contractor has an action against an owner for damages caused by defective plans and specifications.[140] Moreover, modern rules of third-party practice provide that if Bryant had filed suit against the city alone, the city would be able to assert an indemnity claim against its engineer in the same proceeding.[141] Thus, the disputes between the parties could be resolved in a single action.

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135. Bryant also claimed that it was due approximately $90,000 for work performed pursuant to the construction contract. This claim was asserted only against the city. 762 F.2d at 1193 n.1.

136. *See* Annot., *Construction Contractor's Liability to Contractee for Defects or Insufficiency of Work Attributable to the Latter's Plans and Specifications*, 6 A.L.R.3d 1394, 1397-1403 (1966).

137. 160 N.Y. 72, 54 N.E. 661 (1899).

138. *Id.* at ___, 54 N.E. at 664.

139. Greater Richmond Civic Recreation, Inc. v. A.H. Ewing's Sons, Inc., 200 Va. 593, 106 S.E.2d 595 (1959).

140. *See, e.g.*, Mayor & City Council of Columbus v. Clark-Dietz & Assocs.-Eng'rs, Inc., 550 F. Supp. 610, 625 (N.D. Miss. 1982); Worley Bros. Co. v. Marcus Marble & Tile Co., 209 Va. 136, 161 S.E.2d 796 (1968).

141. Alternatively, as Justice Deckle observed in his *Moyer* dissent, the city could defend the claim and, if unsuccessful, assert an indemnity claim against its engineer. *See supra* note 73 and accompanying text.

However, the tripartite proceeding would not be a free-for-all with every party involved in the project asserting negligence claims against one another.[142] The contractor/owner contract would govern whether the contractor could recover, and the owner's claim for indemnity from the engineer would be based on the owner/engineer contract.

Of course, the sequence of parties could be reversed. An engineer might claim that because of a contractor's poor performance (*e.g.*, taking an extra six months to complete its work) the engineer is entitled to delay damages. If the economic loss rule is applied, the engineer's claims would be against the owner and thus the owner/engineer contract would govern. Again, the owner would decide whether to file a third-party claim against the contractor. Since the respective contracts would govern any dispute, the intentions of the parties would be carried out.

CONCLUSION

Bryant Electric, *Blake Construction* and *Moorman* suggest that the boundaries of tort and contract are becoming sharper than they were in the decade after *A.R. Moyer, Inc. v. Graham.* Courts are beginning to give greater emphasis to the basic social policies underlying commercial transactions and less to expanding the domain of tort law. Further development of the doctrine confining the recovery of economic losses within the basic fabric of contract law promises to provide for less uncertainty in commercial transactions, less litigation, and a more efficient marketplace.

142. Gilbane Bldg. Co. v. Nemours Found., 606 F. Supp. 995 (D. Del. 1985) was such a free-for-all. In *Gilbane* two subcontractors filed contract actions against their prime contractor. The prime contractor filed counterclaims against the subcontractor and third-party complaints against the owner, architect and mechanical engineer. The owner then filed claims against the contractor and the subcontractors. The subcontractors then filed claims against the owner. *Id.* at 997-98. The court described the proceedings as "a complex and entangled thicket of litigation . . . ." *Id.* at 997. Nevertheless, the court refused to apply the economic loss rule to eliminate the tort claims. *Id.* at 1001-06.