The scenario is perhaps all too familiar on large construction projects.

Errors in the project design, an engineer's unreasonable rejection of materials or an architect's delay in approving submittals increase the contractor's cost of construction. The general contractor can look to the owner for compensation, but the owner–contractor agreement often contains provisions (such as a "no damage for delay" clause) limiting the contractor's recovery. Can the contractor circumvent the owner and recoup its full costs directly from the design professional in tort?

There has been a flood of recent decisions across the country analyzing that issue. Unfortunately, quantity has not created clarity—the case law is hard to reconcile and often contradictory.

For the most part, the confusion stems from the convergence of two unrelated legal trends:

- the general deterioration of the privity requirement, which has encouraged contractors to sue design professionals despite the lack of a contract between them.
- the judicial desire to prevent tort principles from undermining contractual arrangements, which generally has led to limitations on claims against design professionals for economic losses.

In short, one trend has liberalized the requirements for suing design professionals, and the other threatens to eliminate such suits altogether.

Arizona's Abolishment of the Privity Requirement

Historically, the absence of contractual privity doomed cases brought by Arizona contractors against architects and engineers. In *Blecick v. School Dist.*,[1] for example, the court held that an architecture firm was not liable in tort to the project contractors for the preparation of defective plans and specifications. Due to the lack of privity, the court concluded that the architects' performance obligations were owed solely to the school district, not to the contractors.

One consequence of the privity requirement was to force Arizona contractors to look to the owner for redress. Rather than sue the architect in tort for a defective design, for example, the general contractor would sue the owner in contract for breaching its implied warranty to provide adequate plans and specifications.[2] The owner could then turn to the architect for reimbursement of damages arising out of the architect's defective plans.

The privity rule, however, was abandoned in *Donnelly Construction Co. v. Oberg/Hunt/Gilleland*.[3] There, the Arizona Supreme Court expressly held that the lack of privity between a contractor and an architect did not bar an action against the architect for negligent design. According to the Court, the lack of privity did not *per se* mean that the contractor's harm was unforeseeable to the architect. Rather, the Court found it "foreseeable in the instant case that [the general contractor], hired to follow the plans and specifications prepared by [the architect], would incur increased costs if those plans and specifications were in error."[4]

Thus, under *Donnelly*, contractors in Arizona may pursue claims directly against design professionals. The court did not explicitly decide whether contractors may recover purely economic damages.

Arizona Has Adopted the Economic Loss Doctrine

The so-called economic loss doctrine bars recovery in tort when a plaintiff claims purely economic damages. Its purpose is to maintain the distinction between those claims properly brought in contract from those brought in tort. Or, to put it slightly differently, it is "founded on the theory that parties to a contract may allocate their risks by agreement and do not need the special protection of tort law to recover for damages caused by a breach of contract."[5]

Shortly after the *Donnelly* decision, the Arizona Supreme Court adopted the economic loss rule in *Salt River Project v. Westinghouse Elec. Corp.*[6] There, the Court identified three factors as controlling when a plaintiff is limited to contractual remedies:

- the nature of the defect
- the manner in which the loss occurred
- the type of loss or damage

If the only loss is non-accidental or a party's contract expectations are frustrated, then the remedy is in contract; where a party is physically harmed due to a sudden occurrence—like an explosion—the remedy is in tort.[7]

Since adopting the economic loss rule, Arizona appellate courts have not directly addressed whether claims by contractors against design professionals for economic damages (the issue presented in *Donnelly*) are affected. Other courts from around the country, however, have addressed the question, with three distinct lines of cases emerging:

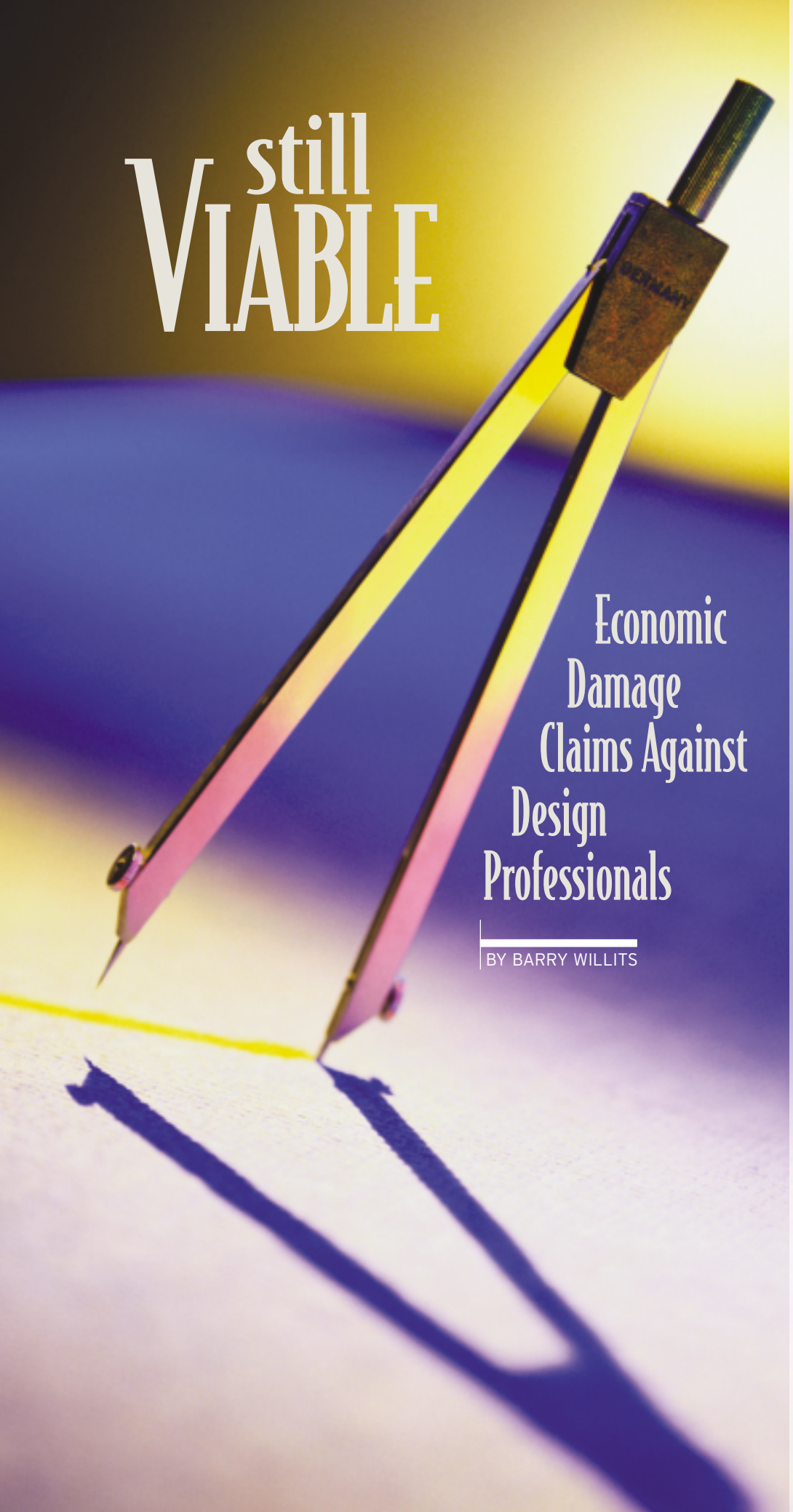
1. cases where the economic loss rule always bars contractors' claims for economic damages
2. cases where the rule sometimes bars based on the relationship between the contractor and the design professional
3. cases where the rule does not bar such claims

I. Claims Always Barred

In a number of cases, the economic loss rule was invoked to bar claims by contractors against design professionals.[8]

The rationale of these cases is generally that the parties on a construction project allocate risks associated with the work through an intricate set of contracts. Therefore, contract law, not tort law, is best suited to measuring those risks. In other words, even though a contractor has no direct contract with the design professional, the contractor still has "the opportunity to allocate the risks associated with the costs of the work when it contracted with the [owner]."[9]

Curiously, these cases also say that such claims would be allowed if there was privity of contract between the architect and the contractor.[10] This is counterintuitive, to say the least, because the very people who are most likely to allocate risks by



contract—the parties to a contract—are apparently able to sue in tort.

In any event, if the concern is preserving the sanctity of contractual obligations on a construction project, then the contractor probably will not be able to circumvent a no-damages-for-delay clause by suing the architect directly.

2. Claims Sometimes Barred

Other cases use a case-by-case approach to determine when application of the economic loss rule is appropriate. These cases will apply the economic loss rule unless the parties are in privity or the relationship between the contractor and the designer approaches privity or is otherwise "special."[11]

To determine whether a sufficient nexus exists between the designer and contractor, these courts "look to the degree of control the design professional exerted over the project and the amount of interaction between the design professional and the third party."[12] Direct supervision of the contractor's work usually is sufficient to create a privity-like nexus. By contrast, merely selling a design that is ultimately built by a contractor is not.

3. Claims Not Barred

Finally, a number of cases have held that the economic loss rule does not bar claims by contractors against design professionals.[13] The rationale of these cases focuses on the interdependence of the various parties on a construction project and the design professional's control over the project. As the Florida Supreme Court put it, "Altogether too much control over the contractor necessarily rests in the hands of the supervising architect for him not to be placed under a duty imposed by law to perform without negligence his functions as they affect the contractor."[14]

These cases also point to Section 552 of the RESTATEMENT (SECOND) OF TORTS, which says:

> One who, in the course of his business, profession or employ-

ment, or in any other transaction in which he has a pecuniary interest, supplies false information for the guidance of others in their business transactions, is subject to liability *for pecuniary loss* caused to them by their justifiable reliance upon the information, if he fails to exercise reasonable care or competence in obtaining or communicating the information.[15]

Significantly, the *Donnelly* court quoted Section 552 with approval, implying that—at least at that time—claims for economic losses were not barred in Arizona.

The Future is Unclear

If there is an emerging consensus, it seems to be that damages for purely economic loss cannot be recovered by contractors against design professionals in the absence of privity or a privity-like relationship. Still, in Arizona, the lack of privity does not appear to be an obstacle so long as *Donnelly* remains good law.

And *Donnelly* is as alive as ever. Last year, for example, Arizona courts expanded *Donnelly* into the legal services context by holding that a lack of privity did not prevent a non-client from suing a lawyer.[16] In fact, the Arizona Supreme Court wrote, "If design professionals cannot escape liability to foreseeably injured third parties who, although lacking privity, are harmed by a designer's negligence, we cannot see why lawyers should not likewise be held to a similar standard."[17]

Thus, at least for now, the economic loss rule appears unlikely to significantly limit claims by contractors against design professionals for economic injuries.

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endnotes

1. 406 P.2d 750 (Ariz. Ct. App. 1965).
2. *See Chaney Building Co. v. City of Tucson*, 716 P.2d 28, 31 (Ariz. 1986); *Kubby v. Crescent Steel*, 466 P.2d 753 (Ariz. 1970).
3. 677 P.2d 1292 (Ariz. 1984).
4. *Id*. at 1296.

5. *Rissler & McMurry Co. v. Sheridan Area Water Supply Bd.*, 929 P.2d 1228, 1235 (Wyo. 1996).
6. 694 P.2d 198 (Ariz. 1984).
7. *See also Apollo Group, Inc. v. Avnet*, 58 F.3d 477 (9th Cir. 1995) (construing Arizona law to bar a purchaser's negligent misrepresentation claim against a seller; the claim essentially amounted to frustrated contract expectations); *Colberg v. Rellinger*, 770 P.2d 346 (Ariz. Ct. App. 1988) (purchaser's tort claims against seller barred).
8. *Fireman's Fund Ins. Co. v. SEC Donohue, Inc.* 679 N.E.2d 1197 (Ill. 1997) (involving claim by subcontractor); *Spancrete, Inc. v. Frazier & Assocs.*, 630 So.2d 1197 (Fla. Dist. Ct. App. 1994) (claim by subcontractor); *Fleischer v. Hellmuth Obata & Kassabaum,* 870 S.W.2d 832 (Mo. Ct. App. 1993) (claim by construction manager against architect); *Tomb & Assocs., Inc. v. Wagner*, 612 N.E.2d 468 (Ohio Ct. App. 1992) (claim by general contractor); *Berschauer/Phillips v. Seattle School Dist.*, 881 P.2d 986 (Wash. 1994) (claim by general contractor); *Rissler & McMurry Co.*, 929 P.2d at 1228 (claim by general contractor).
9. *Rissler & McMurry Co.,* 929 P.2d at 1235.
10. *See Fleischer,* 870 S.W.2d at 836–837.
11. *Ohio Plaza Assocs., Inc. v. Hillsboro Assocs.,* 1998 WL 394370 (Ohio Ct. App. 1998) (designer did not have sufficient nexus to subsequent purchaser of shopping center); *Clevecon v. Northeast Ohio Regional Sewer Dist.*, 628 N.E.2d 143 (Ohio Ct. App. 1993) (architect's participation in project sufficient to create a privity-like nexus with contractor); *Foster Wheeler Enviresponse, Inc. v. Franklin County Convention Facilities Auth.*, 621 N.E.2d 410 (Ohio 1993) (because contractor had a wide range of interactions with the designer, it could maintain a tort suit for economic damages); *Griffin Plumbing & Heating v. Jordan,* 463 S.E.2d 85 (S.C. 1995) (engineer's participation in project created a "special relationship" to contractor).
12. *Ohio Plaza Assocs.*, 1998 WL 394370 at *5.
13. *Eastern Steel Constructors, Inc. v. City of Salem,* 549 S.E.2d 266 (W. Va. 2001); *Jim's Excavating Serv. v. HKM Assocs.,* 878 P.2d 248 (Mont. 1994) (claim for negligent design and negligent supervision of project). *But see Debcon, Inc. v. City of Glasgow,* 28 P.3d 478 (Mont. 2001) (designer did not owe duty to unsuccessful bidder on public works project); *A.R. Moyer, Inc. v. Graham*, 285 So.2d 397 (Fla. 1973).
14. *A.R. Moyer, Inc.*, 285 So.2d at 401.
15. Emphasis added; *but see* RESTATEMENT (SECOND) OF TORTS § 766C ("One is not liable to another for pecuniary harm not deriving from physical harm to the other, if that harm results from the actor's negligently … interfering with the other's performance of his contract or making the performance more expensive or burdensome").
16. *Paradigm Ins. Co. v. Langerman Law Offices, P.A.,* 24 P.3d 593 (Ariz. 2001); *Kremser v. Quarles & Brady, L.L.P.,* 36 P.2d 761 (Ariz. Ct. App. 2002).
17. *Paradigm Ins. Co.,* 24 P.3d at 601.