CROSS CURRENTS IN PROFESSIONAL LIABILITY:
Negligence, Negligent Misrepresentation, Breach of Contract and the Economic Loss Rule in Construction Litigation With Design Professionals

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1. Introduction

In the past several years, our Supreme Court has tended to look to contract principles to resolve disputes involving the performance of contracts, and generally has reversed the trend of their immediate predecessors to apply tort law to contract disputes. At the same time, however, our Court adopted the Restatement of Torts § 552 tort of "Negligent Misrepresentation," which, unless carefully applied, may operate to reintroduce tort law into what are essentially contract disputes.

The economic loss rule and the tort of negligent misrepresentation are cross currents in the law of professional liability, which can have significant effects upon the resolution of disputes involving design professionals. They exemplify the tension between tort and contract law, which has been described as one of the "border wars between and among American law's basic paradigms." William Powers, Jr.*, Border Wars,* 72 Tex. L. Rev. 1209, 1209 (1994); *Crawford v. Ace Signs, Inc.*, 917 S.W.2d 12, 13 (Tex. 1994).

This paper explores the historical antecedents of these currents, and attempts to reconcile them in their application to construction litigation.

II. Economic Loss Rule

> "When the only loss or damage is to the subject matter of the contract, the plaintiff's action is ordinarily one of contract." *Southwestern Bell Tel. Co. v. DeLanney*, 809 S.W.2d 493, 494 (Tex. 1991).

Simply stated, the rule provides that economic damages are not ordinarily recoverable in negligence actions when unaccompanied by physical property damage or bodily injury.

F. Malcolm Cunningham, Jr. and Amiel Fischer, *The Economic Loss Rule: Deconstructing the Mixed Metaphor in Construction Cases*, 33 Tort & Ins. L.J. 147, 149 (1997). The rule itself is, however, a shorthand description for at least three related but separate "economic loss rules":

1. Product Liability Economic Loss Rule (Parties in Privity of Contract):

Economic loss resulting from a product with defective workmanship and materials is not recoverable in tort. *Mid-Continent Aircraft Corp. v. Curry County Spring Service, Inc.,* 572 S.W.2d 308 (Tex. 1978)*; cf. Jim Walter Homes, Inc. v. Reed,* 711 S.W.2d 617 (Tex. 1986).

B. Contract Economic Loss Rule (Parties in Privity of Contract):

If the parties have entered into a contract with each other, the obligations of the contract cannot be relied upon to establish an action in tort for the recovery of purely economic damages unless there is a separate "independent tort." *DeLanney, supra,* and *Crawford v. Ace Signs, Inc.*, 917 S.W.2d 12 (Tex. 1994) are examples of the operation of this rule. The "Independent torts" which have been recognized as exceptions to the rule include the following:

5. Fraud in the Inducement.

The "legal duty not to fraudulently procure a contract is separate and independent from the duties established by the contract itself." *Formosa Plastics Corp. USA v. Presidio Engineers & Contractors, Inc.,* 960 S.W.2d 41, 46 (Tex. 1996).

6. Injury to Other Property.

In *Montgomery Ward & Co. v. Scharrenbeck,* 204 S.W.2d 508 (Tex. 1947), the Supreme Court noted that a repairman whose negligence resulted in burning down the plaintiff's home could be sued for negligence, even though he had a contract with the plaintiff. *Scharrenbeck*--as well as its progeny, which are exhaustively analyzed in Powers & Niver, *Negligence, Breach of Contract, and the "Economic Loss Rule,"* 23 Tex. Tech. L. Rev. 477 (1992)--either involved physical damage to property or can be explained on grounds independent of the economic loss rule.

7. Good Faith and Fair Dealing.

"Absent a 'special relationship,' the duty to act in good faith is contractual in nature, and its breach does not amount to an independent tort." *Crim Truck & Tractor Co. v. Navistar Int'l Transp. Corp.,* 823 S.W.2d 591, 595 n.5 (Tex. 1992).

The Supreme Court has been reluctant to extend the duty of good faith and fair dealing to contexts other than the special relationship between an insurance company and its insured, and indeed has declined even to extend the duty to the relationship between a surety and its principal. See *Associated Indemnity Corp. v. CAT Contracting, Inc.,* 964 S.W.2d 276, 280 (Tex. 1998). The duty has not been extended in construction cases. See *Electro Associates, Inc. v. Harrop Construction Co., Inc.,* 908 S.W.2d 21, 22 (Tex. App. -- Houston [1st Dist.] 1995, writ denied) (contractor/subcontractor relationship).

4. Professional Negligence.

a. In *DeLanney, supra*, the court inserted a now-famous footnote to its opinion adopting the contract economic loss rule: "Of course, some contracts involve special relationships that may give rise to duties enforceable as torts, such as professional malpractice" (emphasis added). *DeLanney, supra*, at 494.

b. Professor Powers believes that the professional negligence cases are best resolved using contract principles. Powers & Niver, *supra*, 23 Tex. Tech L. Rev. at 496, and this is the rationale behind the decision in *CBI NA-COM, Inc. v. UOP, Inc.,* 961 S.W.2d 336, 340 (Tex. App. -- Houston 1st Dist.] 1998, writ denied). ("Because [owner's] claim, if any, [against a designer] would have been for negligent performance

of the contract, its claim against [the designer] would have been limited to a breach of contract claim.")

5. Negligent Misrepresentation.

a. Negligent misrepresentation may or may not be an "independent tort" exception to the contract economic loss rule. In *DSA, Inc. v. Hillsboro I.S.D.,* 973 S.W.2d 662, 663 (Tex. 1998), the court held that the plaintiff's negligent misrepresentation claim failed "for lack of any independent injury," but the holding may have been limited to the damages alleged by the plaintiff.

b. The courts of appeal appear to be split on the issue. See, *Airborne Freight Corp., Inc. v. C.R.. Lee Enterprises, Inc.*, 847 S.W.2d 289, 295 (Tex.App.-- El Paso 1999, writ denied). ["Negligent misrepresentation is a cause of action recognized in lieu of a breach of contract claim, not usually available where a contract was actually in force between the parties."] But see, *Mattheissen v. Schaefer,* 900 S.W.2d 792 (Tex. App. -- San Antonio 1995, writ denied) [survey case, but which may be better explained as a third-party negligent misrepresentation claim].

C. Negligence Economic Loss Rule:

1. Claims for economic loss unaccompanied by physical damage to a proprietary interest are not recoverable in a negligence action. *cf Louisiana, ex rel. Guste v. M/V Test Bank,* 752 F.2d 1019, 1022 (5th Cir. 1985) cert. denied 477 U.S. 903 (1986), citing *Robins Dry Dock v. Flint,* 275 U.S. 303 (1927) (Holmes, J.).

a. Our Supreme Court appears to endorse this rule. In *McCamish, Martin, Brown & Loeffler v. F.E. Appling Interests*, 991 S.W.2d 787 (Tex. 1999) at 790, the court drew a distinction between cases of legal malpractice, "which are subject to the privity rule [which would preclude a non-client from recovering for negligence], and cases of negligent misrepresentation, which are not."

b. *Thomson v. Espey Huston & Associates, Inc.,* 899 S.W.2d 415 (Tex. App. -- Austin 1995, no writ) illustrates this distinction in a construction case. There, the court distinguished between acts of negligence which caused physical damage to property [which were recoverable, under a negligence theory] and purely economic losses unaccompanied by physical damage to property, which were not. Cf. *Bernard Johnson, Inc. v. Continental Constructors Inc.,* 630 S.W.2d 365 (Tex. App.--Austin, 1982, no writ)

(no duty by architect to protect a contractor from the economic losses allegedly caused it by the architect's negligent performance of its contract with the owner); *Higbie Roth Constr. Co. v. Houston Shell & Concrete,* 1 S.W.3d 808, 812 (Tex. App. -- Houston [1st Dist.] 1999, n.w.h.) (subcontractor owed no duty to protect contractor from economic losses [increased worker's compensation premiums] attributable to its negligence).

III. The Tort of Negligent Misrepresentation

1. The Restatement (Second) of the Law of Torts (1977)

The harshness of the negligence economic loss rule has been softened, considerably, by the advent of the "Tort of Negligent Misrepresentation," as defined by the American Law Institute:

> **Section 552. Information Negligently Supplied for the Guidance of Others.**
>
> "(1) One who, in the course of his business, profession or employment, 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.
>
> (2) Except as stated in Subsection (3), the liability stated in subsection (1) is limited to loss suffered
>
> (a) by the person or one of a limited group of persons for whose benefit and guidance he intends to supply the information or knows that the recipient intends to supply it; and
>
> (b) through reliance upon it in a transaction that he intends the information to influence or knows that the recipient so intends or in a substantially similar transaction.
>
> (3) The liability of one who is under a public duty to give the information extends to loss suffered by any of the class of persons for whose benefit the duty is created, in any of the transactions in which it is intended to protect them."

Section 552B. Damages for Negligent Misrepresentation.

"(1) The damages recoverable for a negligent misrepresentation are those necessary to compensate the plaintiff for the pecuniary loss to him of which the misrepresentation is a legal cause, including

(a) The difference between the value of what he has received in the transaction and its purchase price or other value given for it; and

(b) pecuniary loss suffered otherwise as a consequence of the plaintiff's reliance upon the misrepresentation.

(2) the damages recoverable for a negligent misrepresentation do not include the benefit of the plaintiff's contract with the defendant."

2. Adoption

Texas courts have agreed with the Restatement's definition, beginning with *Cook Consultants, Inc. v. Larson,* 700 S.W.2d 231, 234 (Tex.App.--Dallas 1985, writ ref'd n.r.e.), and later by the Supreme Court in *Federal Land Bank v. Sloane*, 825 S.W.2d 439, 442 (Tex.1991).

C. Application

The tort has been applied to a broad range of professions, including:

1. Accountants. *Blue Bell v. Peat, Marwick, Mitchell & Co.*, 715 S.W.2d 408, 411-12 (Tex.App.--Dallas 1986, writ ref'd n.r.e.);

2. Real Estate Brokers. *Hagans v. Woodruff*, 830 S.W.2d 732, 736 (Tex.App.-- Houston 1992, no writ);

3. Auditors. *Steiner v. Southmark Corp.*, 734 F.Supp. 269, 279-80 (N.D. Tex. 1990);

4. Surveyors. *Cook Consultants, supra*;

5. Lawyers. *McCamish, Martin, Brown & Loeffler v. F.E. Appling Interests*, 991 S.W.2d 787, 791 (Tex. 1999).

4. Interpretation

1. "A typical negligent misrepresentation case involves one party to a transaction receiving and relying on an evaluation...prepared by another party's [professional]" *McCamish, supra* at 793;

2. Of existing facts. *Allied Vista, Inc. v. Holt*, 987 S.W.2d 138, 141 (Tex.App.-- Houston [14th Dist.] 1999, n.w.h.; *Airborne Freight Corp. v. Lee*, 847 S.W.2d 289, 294 (Tex.App.--El Paso 1994, writ denied);

3. "Liability is not based on the breach of duty a professional owes his or her clients or others in privity, but on an independent duty to the non-client based on the professional's manifest awareness of the non-client's reliance on the misrepresentation and the professional's intention that the non-client so rely." *McCamish, supra* 991 S.W.2d at 792.

4. Nevertheless, "In determining whether section 552's justifiable reliance element is met, one must consider the nature of the relationship between the [professional, here an attorney] and client, and non-client. *McCamish, supra* 991, S.W.2d at 794.

IV. Application to Architect/Engineer Disputes

The remainder of this paper will attempt to apply the legal principles underlying negligence, contract, and negligent misrepresentation causes of action to two different "garden variety" construction disputes, and attempt to reconcile the Texas cases that have addressed them:

A. Poorly Drawn Plans.

The owner hires an architect who prepares drawings which, when the contractor attempts to execute the work, prove to be inadequate for construction, causing the contractor to suffer economic losses, including extended overhead. Pursuant to the terms

of its general contract with the owner, the contractor is able to recover some--but not all--of its losses through an adjustment of the contract price. Is the architect liable to either the owner or to the contractor for their economic damages?

1. Owner v. Architect

1. Breach of Contract

1. Standard of Care.

If the parties' contract is a standard form of agreement between owner and architect, AIA Form B-141 (1997 edition), there is no standard of care set forth in the contract, and indeed the possibility of negligently prepared drawings is not clearly addressed. Nevertheless, the contract does require that the architect "shall respond in the design of the project to requirements imposed by governmental authorities" (¶ 1.2.3.6) and that his construction documents "shall set forth in detail the requirements for construction of the project" (¶ 2.4.4.1). The production of defective drawings arguably would be a breach of these terms of the contract.

2. Common Law.

Texas courts have implied an obligation for the architect to "...use the skill and care in the performance of his duties commensurate with the requirements of his profession." *IOI Systems, Inc. v. City of Cleveland, Tex.* (Tex. App.--Houston [1st Dist.] 1980, writ ref'd n.r.e.); *Ryan v. Morgan Spear Associates, Inc.,* 546 S.W.2d 678 (Tex. App.-- Corpus Christi 1977, writ ref'd n.r.e.); Powers & Niver, *Supra,* 23 Tex. Tech. L. Rev. at 493 (noting that "the mere fact that courts imply provisions in contract when the parties are silent does not, *ipso facto*, render a breach of that provision a tort. Moreover, the mere fact that the content of the implied promise is similar to negligence does not mean that a breach of the standard is necessarily a 'cause of action' for negligence").

3. Other Contractual Terms.

Resolving the owner/architect dispute under contract principles can be somewhat problematic for the owner, particularly if he is using an AIA form. The standard form of agreement between owner and architect is a product of the AIA's Practice and Prosperity Initiative, and is unabashedly pro-architect. It includes, among

other things, a waiver of claims for consequential damages and a mandatory arbitration clause.

2. DTPA

"Nothing in this subchapter [the DTPA] shall apply to a claim for damages based on the rendering of a professional service, the essence of which is the providing of advice, judgment, opinion or similar professional skill." Tex. Bus. & Com. Code Ann. § 17.49(c) (Supp. 1999).

c. Implied Warranty.

Texas law does not recognize a cause of action for breach of an implied warranty of professional services. *Murphy v. Campbell*, 964 S.W.2d 265, 268 (Tex. 1998); *Parkway Co. v. Woodruff,* 901 S.W.2d 434, 439 (Tex. 1995).

d. Professional Negligence.

1. As noted in the discussion in ¶ II.B., *supra*, a claim for professional negligence between parties to a contract may be barred by the "contract economic loss rule," unless it is recognized as an "independent tort" exception to that rule. See, cf*, DSA, Inc., supra*, 973 S.W.2d at 663.

2. The high water mark of the contract economic loss rule in Texas construction cases is *Thomson v. Espey Huston & Associates, Inc.,* 899 S.W.2d 415, 421 (Tex. App. -- Austin 1995, no writ). There, the engineer's alleged negligence in the performance of its contract was not actionable, outside its contract, because "Espey's performance under the contract, however negligent, could violate only a contractual duty unless, as in *Scharrenbeck*, the negligence caused damage beyond the subject of the contract itself." *Thomson, supra,* 899 S.W.2d at 421. To the extent that the plaintiff was able to claim damages to physical injury to property that was outside the contract, it was able to state a claim; to the extent, however, that the buildings which were the subject of the contract were defective, the court held that Espey's breach of contract did not rise to a tort cause of action. *Id.* But see, *Coulson v. Lake L.B.J. Municipal Utility District,* 734 S.W.2d 649 (Tex. 1987).

3. A potentially significant decision interpreting the contract economic loss rule and the effect of parties' contractual limitation of remedies is *CBI NA-COM, Inc. v. UOP, Inc.,* 961 S.W.2d 336 (Tex. App. -- Houston [1st Dist.] 1998, writ denied). There, the designer furnished the owner with engineering designs for a refinery, pursuant to a contract which limited the designer's liability for negligent designs to

reperforming [redesigning] its work, and specifically disclaimed liability for consequential damages. The owner then entered into a separate contract with a contractor to build the refinery. The owner subsequently sued the contractor for negligence, and the contractor filed a third-party claim for contribution against the designer for contribution.

The court noted that the contractor could only maintain a contribution claim against the designer if the designer was potentially liable to the owner for negligence. The court held that the designer could not be liable to the owner for negligence, because if the owner had sued the designer, "its claims would be limited to economic injury dealing with the subject matter of the contract itself. When a negligence claim is made alleging the breach of the varied duties encompassed in a contract between the parties, the action is for breach of contract and not tort." *CBI NA-CON, supra,* 961 S.W.2d at 340.

3. Negligent Misrepresentation.

1. Can a negligent misrepresentation claim be maintained between parties to a contract?

a. In *D.S.A., Inc. v. Hillsboro I.S.D.,* 973 S.W.2d 662 (Tex. 1998), the defendant was sued for negligent misrepresentations which allegedly induced the plaintiff to enter into the contract. The defendant contended that the negligent misrepresentation claim could only be brought as a breach of contract action. The Supreme Court, in a *per curium* opinion, avoided the issue by holding that the plaintiff's claims essentially were for the benefit of its bargain and, therefore, the plaintiff did not suffer the "independent injury" required in *Formosa Plastics, supra,* 960 S.W.2d 41.

b. *Airborne Freight Corp. v. C.R. Lee Enterprises*, Inc., 847 S.W.2d 289, 295 (Tex.App. -- El Paso 1992, writ denied). ("Negligent misrepresentation is a cause of action recognized in lieu of a breach of contract claim, not usually available where a contract is actually in force between the parties.")

2. Are inadequately prepared drawings "negligent misrepresentations?"

a. "One who...supplies false information for the guidance of others...is subject to liability for pecuniary loss caused to them by their justifiable reliance upon the information." Restatement (2^{nd}) of Torts § 552 (1) (1977) (emphasis added). This language might exclude first party claims.

b. "The sort of 'false information' contemplated in a negligent misrepresentation case is a misstatement of existing fact, not a promise of future conduct." *Allied Vista, Inc. v. Holt*, 987 S.W.2d 138, 141 (Tex.App.-- Houston [14th Dist.] 1999, m.w.h.); *Airborne Freight, supra*, 847 S.W.2d at 294.

2. Contractor v. Architect.

1. Breach of Contract.

The contractor typically is not in privity of contract with the architect, and indeed the AIA A-201 General Conditions ¶ 1.1.2, and the B-141 ¶ 1.3.7.5 both specifically state that nothing contained in either agreement shall "create a contractual relationship of any kind between the Architect and Contractor." This effectively negates the possibility of the contractor bringing the claim as a third-party beneficiary of the architect's contract with the owner, which eliminates his opportunity for bringing a breach of contract claim against the architect. See *Thomson, supra*, 899 S.W.2d at 419; *Bernard Johnson, Inc., supra,* 630 S.W.2d at 369-70.

2. Negligence.

Since the claim is for purely economic loss, it would appear to be barred by the negligence economic loss rule. This appears to be at least implied by *McCamish, supra*, 991 S.W.2d at 791 ("...the general rule [is] that persons who are not in privity with an attorney cannot sue the attorney for legal malpractice"); c.f., *Bernard Johnson, supra,* 630 S.W.2d at 374; and *Thomson, supra*, 899 S.W.2d at 421).

3. Negligent Misrepresentation.

The clear import of the decision in *McCamish, supra* is that an action for negligent misrepresentation can be maintained for economic losses suffered by a limited class of injured parties, even when their damages are solely economic. While other courts of appeal had held otherwise, see e.g., *Thomson, supra*, 899 S.W.2d at 422 ("Thomson's tort causes of action for negligent misrepresentation and fraud derived from the...contract are also barred by the economic loss rule"), at least that portion of the *Thomson* opinion is highly suspect. Assuming that it is possible for a contractor to state a claim against an architect for the tort of negligent misrepresentation, is the tort appropriate to a claim involving defective plans? This involves an examination of the elements of the tort:

1. "One who, in the course of his business, profession..." An architect certainly is in the business.

2. "Supplies false information for the guidance of others in their business transactions..." The comments to the restatement deal primarily with evaluations (e.g., soil reports, discussed below, as opposed to the architect's "instruments of service"). Since "the sort of 'false information' contemplated in a negligent misrepresentation case is a misstatement of existing fact" *Allied Vista, supra*, 987 S.W.2d at 141, the drawings may not fit within the definition.

3. "Is subject to liability for pecuniary loss caused to them..." The contractor's claims are for pecuniary losses.

4. "By their justifiable reliance upon the information..." The contractor arguably is justifiably relying upon the accuracy of the drawings and, although he has a duty to study and compare the drawings before each stage of the work (A-201 ¶s 3.2.1-2, his review is not for the purpose of "discovering errors, omissions, or inconsistencies in the contract documents." Stated differently, there appears to be nothing in the AIA documents which specifically preclude the contractor from relying upon the information furnished by the architect.

On the other hand, the Supreme Court in *McCamish* recognized that a third party's "justifiable reliance" on a representation was not justified if it took place in an adversarial context, and that in determining whether the inter-party relationship was adversarial required an examination of "the extent to which the interests of the client and third party are consistent with each other." *McCamish, supra,* 991 S.W.2d at 794.

While the designer certainly is preparing drawings which it intends to be used for construction, he is doing so pursuant to a contract with the owner, to whom his duty primarily is owed. Should a contractor be entitled to "shoehorn" a cause of action against the designer on the basis of his "reliance" on drawings, when his contract with the owner has been based upon an arm's length transaction?

The Supreme Court suggested in *McCamish* that a defendant could "avoid or minimize the risk of liability to a non-client by setting forth (1) limitations as to whom the representation is directed and who should rely on it, or (2) disclaimers as to the scope and accuracy of the factual investigation or assumptions forming the basis of the representation or the representation itself." *McCamish, supra,* 991 S.W.2d at 795.

Whether disclaimers and limitations of liability contained in the designer's contract with the owner would be effective in limiting the designer's liability

to the contractor is an open question. *CBI NA-COM, Inc., supra* suggests the answer by holding that, at least as between the owner and the designer, the designer can limit its liability by contract, including the imposition of conditions precedent to any claim against the designer and eliminate its liability for negligence. *CBI NA-COM, Inc., supra*, 961 S.W.2d at 340. If the designer can, in his contract with the owner, take his performance out of the ambit of negligence law, is there any reason why a third party should be allowed to avoid the effect of the original parties' contractual undertaking?

5. "If he fails to exercise reasonable care or competence in obtaining or communicating the information." This restatement language is couched in terms of "obtaining" information, which is then "communicated." Query: Do improperly prepared drawings fit within this definition [as opposed to improperly prepared evaluations]?

Indeed, it is difficult to understand why the tort of negligent misrepresentation should apply, at all, to negligently prepared drawings. The owner's contract with the contractor addresses compensation for change orders, and there is nothing to prohibit the owner from addressing it in his contract with the architect, as well. If the possibility that the drawings will require some revision has been addressed in both the Architect's and Contractor's contracts with the Owner, should tort law supply an additional cause of action between the contractor and the architect to address the economic consequences of such revisions?

2. Improper Evaluations/Reports

1. Evaluations of Performance.

Many architectural contracts require the architect, as a representative of the owner, to become generally familiar with the progress and quality of the work and to endeavor to guard the owner against defects and deficiencies in the work. AIA Form B-141 ¶ 2.6.2.1 requires the architect to report to the owner deviations from the contract documents. The failure of the architect accurately to obtain or communicate this information can be a breach of its contract. See, e.g., *Hunt v. Ellisor and Tanner, Inc.,* 739 S.W.2d 933 (Tex. App. -- Dallas 1987, writ denied).

Some states have allowed contractors to assert negligence or negligent misrepresentation claims against the architect or engineer, based upon his faulty evaluations of their performance, but this seems to be doctrinally unsound (the "reliance" element would appear to be lacking) and, in any event, has been repudiated in Texas. *Bernard Johnson, Inc., supra.*

2. Soil Reports and Surveys.

Soil reports and other evaluations of existing conditions are, however, directly within the ambit of the Restatement's view of the tort of negligent misrepresentation. Illustration 9 to Restatement § 552:

> "The City of A is about to ask for bids for work on a sewer tunnel. It hires B Company, a firm of engineers, to make boring tests and provide a report showing the rock and soil conditions to be encountered. It notifies B Company that the report will be made available for bidders as a basis for their bids and that it is expected to be used by the successful bidder in doing the work. Without knowing the identity of any of the contractors bidding on the work, B Company negligently prepares and delivers to the city an inaccurate report, containing false and misleading information. On the basis of the report, C makes a successful bid, and also on the basis of the report, D, a subcontractor, contracts with C to do a part of the work. By reason of the inaccuracy of the report, C and D suffer pecuniary loss in performing their contracts. B Company is subject to liability to C and to D."

Accord, *Cook Consultants v. Larson, supra* (3rd party reliance on incorrect survey).

22. Development of the Law

Our Supreme Court has not directly addressed the intersection of contract, negligence and negligent misrepresentation law in a construction setting. Other states which have done so--and which have directly considered the policies inherent in the application of the economic loss rule--have reached differing results. Some (perhaps a majority) of jurisdictions allow negligent misrepresentation claims brought by contractors against designers. See, e.g., *Tommy L. Griffin Plumbing & Heating Co. v. Jordan, Jones & Goulding, Inc.,* 463 S.E.2d 85 (So. Carolina 1995); *Jim's Excavating Service, Inc. v.*

HKM Associates, 878 P.2d 248 (Montana 1994); *Guardian Construction Co. v. Tetra Tech Richardson, Inc.,* 583 A.2d 1378 (Sup. Ct. Del. 1990); *Moransias v. Heathman,* 744 So.2d 973 (Florida 1999).

A number of other courts have used the economic loss rule to limit design liability in negligent misrepresentation cases: See, e.g., *2314 Lincoln Park West Condominium Association v. Mann,* 555 N.E.2d 346 (Illinois 1990); *Rissler & McMurry Co. v. Sheridan Area Water Supply,* 929 P.2d 1228 (Wyoming 1966) ("We will not allow § 552 to be used as a method to sidestep contractual duties...Therefore, we hold that when the plaintiff has contracted to protect against economic liability caused by the defendant, there is no claim [under § 552] for purely economic loss."); *Berschauer/Phillips Construction Co. v. Seattle School District No. 1,* 881 P.2d 986 (Washington 1994). That court's reasoning is instructive:

> "[B]y limiting the recovery of economic loss due to construction delays to the remedies provided by contract...[we] ensure that the allocation of risk and the determination of future liability is based upon what the parties bargained for in the contract.
>
> * * *
>
> "The fees charged by architects, engineers, contractors...are founded on their expected liability exposure as bargained and provided for in their contract. If we held to the contrary, a party could bring a cause of action in tort to recover benefits they were unable to obtain in contractual negotiations.
>
> * * *
>
> "We acknowledge that § 552 provides support for the recovery of economic damages in the construction industry for negligent

> misrepresentation...We also acknowledge that the tort of negligent misrepresentation is recognized in Washington...We hold that when the parties have contracted to protect against potential economic liability, as is the case in the construction industry, contract principles override the tort principles in § 552 and, thus, purely economic damages are not recoverable." 881 P.2d at 993.

It is impossible confidently to predict which of these conflicting views ultimately will be adopted by our Supreme Court. Nevertheless, it is this author's suggestion that because construction disputes arise in an arena in which the risks of loss are contractually allocated between the parties, it would therefore seem logical that disputes arising out of the parties' performance of their contracts be decided using principles of contract law, with particular reference to the parties' contracts.

The adoption of the tort of negligent misrepresentation should not be allowed to supplant the economic loss rules when either (1) when the parties are in privity of contract with each other or (2) where the remedies for the consequences of another party's failure of contractual performance are governed by the parties' own contracts with the owner. Then, as Professor Powers has noted, "[I]f contractors want to be protected, they can insist on that protection from the owner who will get protection from the architect. The contractors can take less compensation from the owner, so that the owner can in turn compensate the architect for the added risk." Powers & Niver, *supra*, 23 Tex. Tech L. Rev. at 523. Conversely, contractors can demand greater compensation for absorbing the risk of defective drawings, and the owner can reduce the architect's compensation, accordingly.

While this may seem simplistic or naive, it does reflect a contractual allocation of the risk, and "not only encourages the parties to negotiate the limits of liability...but it holds the parties to the terms of their agreement." *Rissler & McMurry Co., supra,* 929 P.2d at 1235.