University of Michigan Journal of Law Reform

Volume 32

1999

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Recommended Citation
Eileen Silverstein, *On Recovery in Tort for Pure Economic Loss*, 32 U. MICH. J. L. REFORM 403 (1999).
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ON RECOVERY IN TORT FOR PURE ECONOMIC LOSS†

Eileen Silverstein*

Pure economic loss is not considered a recoverable harm in tort law. Professor Silverstein asks, "Why not?"

INTRODUCTION

Throughout the law, one discovers that similar consequences are treated differently, depending on whether economic or physical integrity is implicated.[1] For example, getting something valuable for next to nothing by paying subsistence wages to workers is good business practice, while taking a television set from the smashed window of a store is a crime;[2] getting the deal you want by threatening to kill your adversary's children is unlawfully coercive, but pressuring a community to waive millions in taxes as a condition for not moving corporate operations to another state is skillful negotiating;[3] and getting money by pointing a gun at someone is armed robbery, while it is a close question whether making a profit by selling environmentally contaminated land as suitable for residential development to first-time home buyers may be illicit.[4]

The question I wish to explore is the basis for distinguishing between these similar circumstances. Why, in the examples given above, does use of physical coercion make getting something for nothing, getting the deal you want, and getting money unlawful?

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1. I use the term "integrity" to connote wholeness and security. Terminology is difficult, because some doctrines distinguish between economic and physical conduct and others between economic and physical outcomes in evaluating legality.

2. *See* Richard Rothstein, *Who Are The Real Looters?*, DISSENT, Fall 1992, at 429, 429–30 (comparing looters in Los Angeles with various corporate officers).

3. *See* Charter Township of Ypsilanti v. General Motors Corp., 506 N.W.2d 556, 559 (Mich. Ct. App. 1993) (noting that discussions of job creation and retention in connection with solicitations for tax abatements are not promises but "hyperbole and puffery").

4. *See* Lindsey Gruson, *18 Suburban Homes: A Dream Undermined*, N.Y. TIMES, May 13, 1993, at B1. Even where economic coercion is deemed criminal, as in cases of fraud, the penalty for taking money in a financial transaction is significantly less than that for taking money at gunpoint. *See* Thomas Koenig & Michael Rustad, *"Crimtorts" as Corporate Just Deserts*, 31 U. MICH. J.L. REFORM 289, 314 n.109 (1998).

Another way to phrase the question is: What presuppositions about economic and physical integrity does the law embody, and what effects do these presuppositions have on legal outcomes?

The search for an answer begins[5] with an examination of one of tort law's oldest doctrines: Unintentional conduct that causes physical harm to persons and property supports full compensation to the injured party, including consequential damages for lost income, property, and profits; but if the same conduct results in economic harm unaccompanied by physical injury, there is no recovery despite the magnitude of the loss.[6] Thus, if negligent maintenance of a utility transformer causes a telephone pole to lop the chimney from a factory's roof, the utility must bear the costs of repair; if the falling telephone pole separates a person's little finger from her left hand, the utility is liable for her medical expenses, pain and suffering, and lost income. Indeed, if the lopped off chimney costs the factory a few days of production, or if the separated finger causally disables an investor from effecting a FAX transmission authorizing a sale of stock worth $2 million, both losses are recoverable because they are attendant on negligently inflicted damage to person (the broken finger) or property (the damaged chimney). But if, instead of amputating a finger or a chimney, the downed telephone pole merely causes the interruption of a communication authorizing the stock transaction, the investor, not the utility company, must bear the $2 million loss; and if the damaged chimney causes the factory to suspend operations for a few days, while the utility is responsible to the factory owner for repairs and lost profits, it is not responsible to the factory employees for lost wages, since the employees experienced no physical impairment of *their* property or persons.[7]

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5. In a series of essays on unrelated doctrines from tort, contract, criminal, employment, and labor law, I will examine how the question of legality differs depending on whether physical or economic integrity is involved. I call these explorations essays, in Isaiah Berlin's sense of the term: "an essay . . . essays a subject, testing it, running it through an exposition and objections . . . . Such essays do not prove cases. They explore subjects, informally, sometimes playfully, and leave the reader to draw his own conclusions." Robert Darnton, *Free Spirit*, N.Y. REV. BOOKS, June 26, 1997, at 9, 9.

6. *See* Connecticut Mut. Life Ins. Co. v. New York & New Haven Ry., 25 Conn. 265, 274–76 (1856) (denying recovery for economic loss in commercial transactions).

7. *See, e.g.*, FMR Corp. v. Boston Edison Co., 613 N.E.2d 902, 903 (Mass. 1993) (affirming no recovery for lost income and increased costs of doing business following power outage); United Textile Workers of Am. v. Lear Siegler Seating Corp., 825 S.W.2d 83, 87 (Tenn. 1990) (denying recovery for employees' lost earnings following leak at industrial park that caused one-day closing of neighboring facility). For the classic cases, see *Connecticut Mutual*, 25 Conn. at 274–76, which allowed no recovery for economic loss in commercial transactions, discussed *infra* notes 23–26, and *Stevenson v. East Ohio Gas Co.*, 73 N.E.2d 200, 203 (Ohio 1946), which denied recovery of wages, discussed *infra* notes 47–52 and accompanying text.

The intuitive explanation for excluding economic loss "only" from tort liability is that physical injury is more serious than economic injury.[8] Recall the rhetorical demand, "your money or your life," to which the answer—turning over the money—is "a foregone certitude."[9] But, as just described, a negligently maintained utility pole causing a broken little finger supports damages, including consequential loss of income or profits, while the same negligent maintenance causing a failed FAX transmission and a loss of $2 million results in absolutely no liability. Indeed, negligently caused damage to property ranks higher than, and is classified differently from, economic loss:[10] The factory owner's losses from damage to the facility are compensable, whether $500 or $5 million, while the physically uninjured investor's $2 million loss from the failed FAX transmission is not.

Judges and commentators, in explaining tort law's long-standing reluctance to award damages for economic loss "only," acknowledge that unrealized wages and profits are harms, but they emphasize the law's overriding concern with avoiding unlimited liability for accidents associated with socially desirable activity.[11]

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8. *See* Fleming James, Jr., *Limitations on Liability for Economic Loss Caused by Negligence: A Pragmatic Appraisal*, 25 VAND. L. REV. 43, 54 n.45 (1972) ("A number of the participants in the London workshop also felt that the integrity of the body and the integrity of tangible property are entitled to a higher priority in the scale of man's proper values than the integrity of intangible wealth."). Other commentators draw a distinction between injuries to persons and property when explaining the rule against recovery for pure economic loss. *See* P.S. Atiyah, *Negligence and Economic Loss*, 83 LAW Q. REV. 248, 269 (1967) ("It is hardly necessary to labour the point that no form of personal injury can be truly compensated for in money, and it is not surprising that the law affords much greater protection for personal injury than for other forms of loss or injury."); Robert L. Rabin, *Tort Recovery for Negligently Inflicted Economic Loss: A Reassessment*, 37 STAN. L. REV. 1513, 1532 (1985) [hereinafter Rabin, *A Reassessment*] ("[I]t is undeniable that over the course of a century the courts have come to attach particular significance to the problem of personal injury."); *see also* S.M. Wilson & Co. v. Smith Int'l, Inc., 587 F.2d 1363, 1376 (9th Cir. 1978) (stating that to treat a breach of warranty "as an accident is to confuse disappointment [economic loss] with disaster [physical injury]").

9. The phraseology is adapted from ARTHUR C. DANTO, AFTER THE END OF ART: CONTEMPORARY ART AND THE PALE OF HISTORY 86 (1997).

10. *But see infra* text accompanying notes 89–94.

11. *See* Louisiana *ex rel.* Guste v. M/V Testbank, 752 F.2d 1019, 1024–28 (5th Cir. 1985). Some might say that the doctrine's survival helps to prove its intrinsic rightness. The tenacity of an idea, however, cannot be proof of its accuracy: Humans cannot fly unaided like birds, superman's feats notwithstanding. The survival of the doctrine rejecting recovery for pure economic loss must be explained rather than used as evidence of its own validity. Nor is tenacity evidence of rightness in the sense of an efficient solution. Long-term adherence to a rule suggests conforming business practice and predictability, but the argument is circular. Long-term adherence to a competing rule would promote the same evidence of custom and reliance: Pure economic loss, if recoverable in tort, would be a cost of doing business taken into account in design, marketing, pricing, and insuring decisions.

Another explanatory candidate is that the rule aids nascent business development, thought necessary in the nineteenth and early twentieth centuries and carried forward as

Thus, as Justice Cardozo warned, an investor who relied detrimentally on an accounting firm's preparation of a certified balance sheet for its client had no claim against the firm:

> If liability for negligence exists, a thoughtless slip or blunder, the failure to detect a theft or forgery beneath the cover of deceptive entries, may expose accountants to a liability in an indeterminate amount for an indeterminate time to an indeterminate class. The hazards of a business conducted on these terms are so extreme as to enkindle doubt whether a flaw may not exist in the implication of a duty that exposes to these consequences.[12]

As expressed in contemporary policy terms by then-Judge Breyer,[13] "liability for pure financial harm, insofar as it proved vast, cumulative and inherently unknowable in amount, could create incentives that are perverse [if a goal of the tort system is to pro-

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good policy despite the recent emphasis on incentives and risk spreading. *See* MORTON J. HORWITZ, THE TRANSFORMATION OF AMERICAN LAW, 1870–1960, at 13 (1992). This class-based explanation has the virtue of bluntness; the law prefers business interests over individual losses either because promoting economic development is good for society as a whole or because the haves protect their own. One problem with such determinist thinking is that the facts do not fit. During the same period that courts were rejecting claims of negligent interference with contracts because of their bank-busting potential, judges were holding manufacturers responsible for injuries in the absence of privity or fault. *See infra* text accompanying notes 36–41. Moreover, some of the early cases pitted one type of business against another. While the class-based theory may explain the protection of an entrepreneur over a worker, and of accountants (whose profession resembles that of lawyers) over investors, how can we assert that the courts preferred the interests of builders over printers, or of ship owners over time charterers? Undoubtedly in particular cases judges reflected on the impact of liability rules on an immature industry, business, or profession, but the development of legal doctrines must accommodate overlapping demands. *See* George P. Fletcher, *Fairness and Utility in Tort Theory*, 85 HARV. L. REV. 537, 567 n.111 (1972).

Finally, law and economics literature focuses on administrative concerns about multiple lawsuits. *See generally* W. Bishop, *Economic Loss in Tort*, 2 OXFORD J. LEGAL STUD. 1 (1982); Mario J. Rizzo, *A Theory of Economic Loss in the Law of Torts*, 11 J. LEGAL STUD. 281 (1982). *But see* Rabin, *A Reassessment*, *supra* note 8, at 1535 n.72; PETER CANE, TORT LAW AND ECONOMIC INTERESTS 471–72, 487–505 (1991).

12. The language is Justice Cardozo's in *Ultramares Corp. v. Touche*, 174 N.E. 441, 444 (N.Y. 1931), discussed *infra* notes 56–60 and accompanying text. The New York Court of Appeals recently affirmed the *Ultramares* court's holding in *Credit Alliance Corp. v. Arthur Andersen & Co.*, 483 N.E.2d 110, 114–15 (N.Y. 1985), while the New Jersey Supreme Court rejected the *Ultramares* holding in *H. Rosenblum, Inc. v. Adler*, 461 A.2d 138, 145–47 (N.J. 1983), discussed *infra* notes 115–25 and accompanying text.

13. *See* Barber Lines A/S v. M/V Donau Maru, 764 F.2d 50, 55 (1st Cir. 1985). Judge Breyer was joined by Circuit Judge Torruella and Senior Circuit Judge Rosenn of the Third Circuit. *See id.*

mote safe operations]."[14] Accordingly, owners of a vessel that negligently spilled oil into Boston Harbor were not responsible for the "significant" extra labor, fuel, transport, and docking expenditures incurred by a nearby ship forced to alter its docking arrangements.[15]

Fleming James, dubbing this the "pragmatic" objection to recovery for economic loss, generally concurs.[16] Robert Rabin argues that the tort system simply shuns widespread liability however incurred; thus, he groups economic loss along with emotional distress and loss of consortium in the categories of harms for which recovery has been limited expressly to control against liability of indeterminate magnitude.[17] To the extent that Rabin and others detect a softening in the long-standing resistance to recovery for economic loss "only," it is solely (and in their view appropriately so) in those cases featuring loss by identifiable individuals who were the intended beneficiaries of the defendant's activity.[18]

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14. *Id.* Judge Breyer's scholarly opinion also notes the unknowable but predictable increases in the number of claimants and in administrative costs that would burden the litigation system, citing to the law and economics literature. *See id.* More recently, Justice Breyer affirmed the liability limiting rationale underlying the no recovery rule in *Saratoga Fishing Co. v. J.M. Martinac & Co.*, 520 U.S. 875, 882 (1997), this time without citation to the law and economics literature. To respondents' argument about imposing too great a liability in tort, Justice Breyer answered for the majority: "[A] host of other tort principles, such as foreseeability, proximate cause, and the 'economic loss' doctrine, already do, and would continue to, limit liability in important ways." *Id.* at 884.

15. *See Barber Lines*, 764 F.2d at 50. According to the district court opinion, the alleged losses were $150,000. *See* Barbar Lines A/S v. M/V Donau Maru, 615 F. Supp. 109, 110 n.1 (D. Mass. 1984).

16. *See* James, *supra* note 8, at 48–58. Consistent with his general preference for risk-spreading, James cautions that the pragmatic objection to recovery for economic loss should not apply in situations where the likelihood of widespread liability is minimal nor in those circumstances where third-party insurance would be likelier and cheaper than first-party insurance; however, these exceptions are of limited scope, and James seems to take quite seriously the fear of unlimited liability as a reason to deny economic loss recovery in general. On the use of insurability as a factor in deciding questions of liability, see CANE, *supra* note 11, at 456–61.

17. *See* Rabin, *A Reassessment*, *supra* note 8, at 1514–15 ("It is my thesis that an identifiable type of economic loss case raises the specter of *widespread tort liability*—a characteristic which in itself has never been uniquely confined to economic loss situations—and that economic loss cases lacking this feature do not receive distinctive treatment." (emphasis in original) (footnote omitted)).

18. Rabin dubs this the "triangular configuration" and distinguishes the limited, intended class of beneficiaries from a "general category of potential beneficiaries." *Id.* at 1527–28; *accord* W. PAGE KEETON ET AL., PROSSER AND KEETON ON THE LAW OF TORTS § 129, at 1002 (5th ed. 1984). *But see* Robert L. Rabin, *Some Thoughts on the Ideology of Enterprise Liability*, 55 MD. L. REV. 1190, 1202–03 (1996) [hereinafter Rabin, *Enterprise Liability*]. There, Rabin discusses professional negligence cases as an example of broadened liability premised on the ideology of enterprise responsibility for creating risks through the course of ordinary business. *See id.*

I propose a significantly different explanation of tort law's treatment of recovery for stand-alone economic harm. Even though many injuries are potential bank busters, stand-alone economic injuries have been singled out for exemption from recovery not because they are fundamentally different from injury to person and property, but because of their similarity to outcomes in routine market transactions. That is, examination of the economic harm from negligent conduct which involves no physical injury leads one to think about and to make comparisons with economic harm caused by market transactions. Consider three situations: (1) In our hypothetical of the falling telephone pole, in the event of a resulting broken finger, the law inquires in exquisite detail into the level of care undertaken by the utility company in installing and maintaining the transformer. (2) By comparison, if an investor loses $2 million because a corporation's performance does not meet her expectations, the law rarely asks why; and even if the loss is directly attributable to high-level decision-making, such as the marketing of a new product, the law never asks whether company officials exercised reasonable care in deciding to launch the product. (3) Now recall the hypothetical investor who is not physically injured by the falling telephone pole but whose FAX transmission is affected, with the resulting loss of $2 million. If no salient factors distinguish (2) economic harm caused by the market from (3) negligently caused economic loss, either both or neither should be actionable. I suggest that if courts allow recovery for negligently caused pure economic loss, it would be difficult to identify distinguishing, salient factors and to explicate why the market's form of economic injury goes uncompensated. The requirement of (1) *some* injury to person or property effectively eliminates the need to consider the consequential anomalies and similarities of (2) and (3). As I will argue, this explanation for the categorical refusal to recognize an independent claim for economic loss fits the facts as well as other accounts.

Parts I and II of this Essay do the easy work of demonstrating the anomalous position of the economic loss rule in tort doctrine. Part I traces the case law, drawing distinctions between fully compensable injuries resulting from physical harm to persons and property and noncompensable injuries where the loss is solely economic. Surprisingly, the century-old rationale for the categorical bar, the specter of unbounded recovery, continues to be advanced virtually

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The clear majority of jurisdictions require an identifiable, intended beneficiary. *See infra* note 63. This approach is also recommended by the RESTATEMENT (SECOND) OF TORTS 552(2)(a) (1977); Atiyah, *supra* note 8, at 269–76; and James, *supra* note 8, at 43–44.

unexamined despite reconsideration of most tort rules over the last hundred years, despite the continual expansion of grounds for liability, and despite the now commonplace awards of huge, unknowable sums in claims involving physical injuries. Part II illustrates how contemporary principles of tort law could be applied to stand-alone economic injury, with causation and duty undertaking their familiar job of limiting liability.[19] Finally, Part III takes on the hard labor of explaining the remarkable vitality of the unlimited liability rationale for the economic loss doctrine and of challenging the intuitive assumption that interference with economic integrity is not as significant as interference with physical integrity.

I.

The origins of the categorical refusal to award tort damages for pure economic loss are easily identified. Mid-nineteenth century judges formulated rigid rules for deciding disputes and were cautious about extending liability for accidental injuries.[20] As Lawrence Friedman has pithily summarized it:

> By the beginnings of the Gilded Age [1870], the general features of the new tort law were crystal-clear. The leading concepts—fault, assumption of risk, contributory negligence, proximate cause—had been all firmly launched on their careers.... What they added up to was also crystal-clear. Enterprise was favored over workers, slightly less so over passengers and members of the public. Juries were suspected—on thin evidence—of lavishness in awarding damages; they

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19. I am not suggesting that current applications of duty and causation are optimally coherent or logical. The use of duty and causation to set boundaries on liability has the same faults as other policy-generated doctrines. My point is rather that the liability for pure economic loss can be managed, like liability for other harms, using the doctrines of duty and causation. *See, e.g.*, Strauss v. Belle Realty Co., 482 N.E.2d 34, 37–38 (N.Y. 1985) (using privity to cut off liability after a massive power failure in New York).

20. The rule against liability for negligently caused economic loss has its roots in the early denial of claims for negligent interference with contract relations. *See* Charles E. Carpenter, *Interference with Contract Relations*, 41 HARV. L. REV. 728, 737–42 (1928). Economic injury from intentional interference with contract relations was remediable so long as the interference was not justified. *See generally* Harvey S. Perlman, *Interference with Contract and Other Economic Expectancies: A Clash of Tort and Contract Doctrine*, 49 U. CHI. L. REV. 61, 63–97 (1982) (discussing the state of the law and the proper scope of the interference tort). For a critical evaluation, see ROBERT L. HALE, FREEDOM THROUGH LAW: PUBLIC CONTROL OF PRIVATE GOVERNING POWER 55–94 (1952).

> had to be kept under firm control. The thrust of the rules, taken as a whole, approached the position that corporate enterprise should be flatly immune from actions for personal injury.[21]

Friedman hastens to add that this was not a conscious attempt or conspiracy to cut liability: "[T]he spirit of the age was a spirit of limits on recovery. People lived with calamity. . . ."[22]

The germinal decision denying recovery for negligently caused economic loss, *Connecticut Mutual Life Insurance Co. v. New York & New Haven Railway*,[23] perfectly exemplifies this mindset. The plaintiff held a $2,000 life insurance policy on a passenger who was killed through defendant railway company's negligence. In denying the insurance company's claim for economic loss, the court found no duty owed by the railway to the insurance company, an unexceptional determination under then-existing doctrine.[24] Not unlike other liability-limiting decisions at this time,[25] the court then warned of the calamitous effect of holding otherwise:

> Such are the complications of human affairs, so endless and far-reaching the mutual promises of man to man, in business and in matters of money and property, that rarely is a death produced by a human agency, which does not affect the pecuniary interest of those to whom the deceased was bound by contract. To open the door of legal redress to wrongs received through the mere voluntary and factitious relation of a contractor with the immediate subject of the injury, would be to encourage collusion and extravagant cantracts [sic] between men, by which the death of either through the involuntary default of others, might be made a source of splendid profits to the other, and would also invite a system of

21. LAWRENCE M. FRIEDMAN, A HISTORY OF AMERICAN LAW 475 (2d ed. 1985); *see also* Tiller v. Atlantic Coast Line R.R., 318 U.S. 54, 59 (1943) ("Assumption of risk is a judicially created rule which was developed . . . to insulate the employer as much as possible from bearing the 'human overhead' which is an inevitable part of the cost—to someone—of the doing of industrialized business. The general purpose . . . seems to have been to give maximum freedom to expanding industry.").

22. FRIEDMAN, *supra* note 21, at 470; *cf.* HORWITZ, *supra* note 11, at 112 (making a convincing case that judges consciously used the law to advance certain political and economic interests).

23. 25 Conn. 265 (1856).

24. *See id.* at 273–77.

25. *See, e.g.*, Ryan v. New York Cent. R.R., 35 N.Y. 210, 211–13 (1866) (limiting liability from negligently started fire to first destroyed building).

> litigation more portentious [sic] than our jurisprudence has yet known.[26]

Thus, the categorical rule against recovery for pure economic loss and its rationale fit nicely into the emerging jurisprudence of severely circumscribed liability for accidental injuries.

As we know, however, the uncritical commitment to burgeoning enterprise was quickly tempered, and over the last century, courts and legislatures have consistently broadened the bases for liability. In describing these developments, commentators often identify three periods of ferment in tort law: The first shift ameliorated some of tort doctrine's most enterprise-embracing elements;[27] the second extended the bases for liability by allowing claims in the absence of both privity of contract and fault;[28] and the third rejected long-standing limitations on the types of injuries which support recovery.[29] Interestingly, these shifts have had little impact on the rule against recovery for pure economic loss.

Friedman, comparing the initial tort decisions of 1850 with those of the late 1890s, traces the gradual easing of the doctrines used to deny defendants' liability, such as assumption of risk, proximate cause, fault, and contributory negligence. He states: "Reaction to the severe rules made itself felt almost as soon as each restrictive doctrine was born."[30] Fear of excessive liability gave way to impulses of "humane[ness]."[31] Equally, by the 1890s, the "rage of the victims" carried significant political weight:

> Change was clearly on the way. Insurance and risk-spreading techniques were ready; cushions of capital reserves were ready; most important, perhaps, an organized and restless working class pressed against the law with voices and votes. The rules of tort law, in twilight by 1900, were like some great but transient beast, born, spawning and dying in the shortest of time. The most stringent rules lasted, in their glory, two generations at most.[32]

The ameliorating spirit traced by Friedman had no impact on the economic loss doctrine, however. For example, in the often

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26. *Connecticut Mutual*, 25 Conn. at 274.

27. *See infra* text accompanying notes 30–35.

28. *See infra* notes 36–46 and accompanying text.

29. *See infra* notes 74–97 and accompanying text.

30. FRIEDMAN, *supra* note 21, at 476.

31. *Id.* at 485 (quoting Gary Schwartz, *Tort Law and the Economy in Nineteenth-Century America: A Reinterpretation*, 90 YALE L.J. 1717 (1981)).

32. *Id.* at 475–76, 486–87.

cited 1903 case of *Byrd v. English*,[33] the owner of a printing plant lost electrical power for several hours as a consequence of broken wires caused by defendant's negligent excavation of a building site.[34] In denying plaintiff's claim against the builder for economic loss, the court opined:

> If the plaintiff can recover of these defendants upon this cause of action, then a customer of his, who was injured by the delay occasioned by the stopping of his work, could also recover from them, and one who had been damaged through his delay could in turn hold them liable, and so on without limit to the number of persons who might recover on account of the injury done to the property of the company owning the [wires]. To state such a proposition is to demonstrate its absurdity.[35]

Perhaps because the harm in denying recovery for economic loss could not be as dramatically illustrated as the harm in denying recovery for a lost arm, the general loosening of tort's harshest doctrines did not extend to the categorical refusal to recognize pure economic loss. Perhaps most victims of economic loss themselves accepted the inevitability of their status and never experienced or expressed their rage. Perhaps at the end of the nineteenth century the consequences of physical injury appropriately overshadowed the effects of pure economic loss.

Nonetheless, one is left wondering why the *Byrd* court, so creative in conjuring images of a single claim exploding into a multitude of lawsuits, did not pause to address the consequences of denying recovery to the single plaintiff who alone claimed that the interruption of power caused provable damages with reasonable certainty.

Beginning in 1916, a number of tort doctrines changed even more dramatically. Restrictions on liability fell, largely in response to the stunning ability of machines and modern working conditions in the new era of mass production to cause devastating injuries to people and property.[36] Thus, the liability-limiting requirement of privity of contract in order to sue a producer for

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33. 43 S.E. 419 (Ga. 1903).

34. *See id.*

35. *Id.* at 420. The court also cited and quoted *Connecticut Mutual Life Insurance Co. v. New York & New Haven Railway*, 25 Conn. 265 (1856), discussed *supra* notes 23–26 and accompanying text.

36. *See* FRIEDMAN, *supra* note 21, at 467.

injury from a defective product[37] gave way to the rule imposing on manufacturers a duty of care to workers, to consumers, and to passersby, as well as to immediate purchasers.[38] A generation later, the rigid insistence on fault as an indispensable predicate for tort liability[39] found exceptions first for physical injuries caused by inherently dangerous activities and products[40] and then for harms to persons and property sustained in using all sorts of goods.[41] Tort doctrine abandoned privity and fault as gatekeepers to recovery in some circumstances because of the inability of injured parties to protect themselves from the hazards of the modern world and because of the superior capacity of market participants to invest in safety precautions and to internalize the costs of accidents. Put differently, in some contexts the fearsome spectre of endless liability to injured persons and property came to be viewed as a cost of doing business, to be controlled not by categorical restrictions on liability but by thoughtful (and sometimes arbitrary) application of principles of causation and duty.

During this period, academic writers called attention to the logical inconsistency between the rules denying pure economic loss and the rules permitting consequential damages for economic injury associated with personal and property damage, and they argued for reform.[42] But a generation later these same writers

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37. *See* Winterbottom v. Wright, 152 Eng. Rep. 402, 405 (Ex. 1842) (holding barred a suit by an injured coachman against the maker of a defective wheel because of the absence of privity: "if the plaintiff can sue, every passenger, or even any person passing along the road, who was injured by the upsetting of the coach, might bring a similar action").

38. *See* MacPherson v. Buick Motor Co., 111 N.E. 1050, 1053 (N.Y. 1916); *see also* East River S.S. Corp. v. Transamerica Delaval Inc., 476 U.S. 858, 867 (1986) (noting that the manufacturer's duty includes protection against property damage). Rabin argues that the threat of liability for multiple injuries arising from one negligent act was manageable as long as the injuries were to persons but that fear of widespread liability for multiple injuries to property remained strong and that the concept of duty did the work of privity doctrine in containing liability. In support of his reading, Rabin cites the New York fire rule limiting liability to the first building damaged by the negligently caused fire. *See* Rabin, *A Reassessment*, *supra* note 8, at 1529–30. But as Rabin also notes, the New York rule was unique, *see id.* at 1530 n.55, and damage to property generally supports an award of consequential economic loss. On the similar treatment of injury to persons and property in British law, see Atiyah, *supra* note 8, at 269.

39. *See* OLIVER WENDELL HOLMES, JR., THE COMMON LAW 94–96 (1881).

40. *See* KEETON ET AL., *supra* note 18, §§ 76–78 (discussing blasting, animal, and fire cases).

41. *See* Seely v. White Motor Co., 403 P.2d 145, 152 (Cal. 1965) (Traynor, C.J.) ("Physical injury to property is so akin to personal injury that there is no reason for distinguishing them."), *cited with approval in East River*, 476 U.S. at 867. Justice Traynor's earlier, concurring opinion in *Escola v. Coca Cola Bottling Co.*, 150 P.2d 436, 440–44 (Cal. 1944) (Traynor, J., concurring), is the standard citation for the beginning of the movement toward strict liability.

42. *See* James, *supra* note 8, at 46–47.

conceded the continuing asymmetry. Thus, in 1941, William Prosser criticized the rule against recovery for foreseeable economic injury and hesitatingly stated that "[t]here is some slight authority looking rather vaguely in this direction,"[43] only to concede in 1971 that "[t]here is actually, however, very little [case law] looking even vaguely in this direction."[44] Fowler Harper, noting authority to support a rule of liability for negligently inducing a breach of contract or otherwise interfering with contract relations, predicted in 1933 that "[u]ndoubtedly such a result is sound, and it is likely to be followed in future cases,"[45] only to report twenty years later that "as a general rule, liability for negligent interference with contractual relations does not exist."[46]

The leading decision invoking the economic loss doctrine during this period, *Stevenson v. East Ohio Gas Co.*,[47] confirms the continuing vitality of the economic loss doctrine and its rationale. In *Stevenson*, the plaintiff was denied access to his workplace following an explosion attributable to the negligence of East Ohio Gas, which was storing natural gas at Stevenson's place of employment.[48] Conscientiously citing earlier decisions and echoing their speculations about the ripple effects of recognizing a claim for modest, stand-alone economic injury to a single party, the court first observed that if Stevenson stated a cause of action for lost wages, then "each one of the thousands of workmen who lost wages by reason of fire, negligently started,"[49] would have economic loss claims against the negligent tortfeasor. The court further stated:

> Cases might well occur where a manufacturer would be obliged to close down his factory because of the inability of

43. WILLIAM PROSSER, HANDBOOK OF THE LAW OF TORTS 993 (1st ed. 1941).

44. WILLIAM PROSSER, HANDBOOK OF THE LAW OF TORTS 940 (4th ed. 1971).

45. FOWLER V. HARPER, A TREATISE ON THE LAW OF TORTS 477–78 (1933).

46. Fowler V. Harper, *Interference with Contractual Relations*, 47 NW. U. L. REV. 873, 892 (1953). A similar pattern appeared in the jurisprudence of products liability. The California and New Jersey Supreme Courts reached contrary conclusions in 1965 about the recovery of economic loss for defective products. *Compare Seely*, 403 P.2d at 151–52 (no recovery), *with* Santor v. A & M Karagheusian, Inc., 207 A.2d 305, 313–14 (N.J. 1965) (allowing recovery). Twenty years later the New Jersey Supreme Court, responding to the icy reception of federal and state courts, fell in with the majority view and held that a commercial buyer could not sue in products liability for its economic loss. *See* Spring Motors Distrib., Inc. v. Ford Motor Co., 489 A.2d 660, 663 (N.J. 1985). The *Seely-Santor* debate is ably dissected in Gary T. Schwartz, *Economic Loss in American Tort Law: The Examples of* J'Aire *and of Products Liability*, 23 SAN DIEGO L. REV. 37, 51–78 (1986).

47. 73 N.E.2d 200 (Ohio Ct. App. 1946).

48. *See id.* at 201.

49. *Id.*

> his supplier due to a fire loss to make prompt deliveries; the power company with a contract to supply a factory with electricity would be deprived of the profit which it would have made if the operation of the factory had not been interrupted by reason of fire damage; a man who had a contract to paint a building may not be able to proceed with his work; a salesman who would have sold the products of the factory may be deprived of his commissions; the neighborhood restaurant which relies on the trade of the factory employees may suffer a substantial loss. The claims of workmen for loss of wages who were employed in such a factory and cannot continue to work there because of a fire, represent only a small fraction of the claims which would arise if recovery is allowed in this class of cases.[50]

Of course, as the court noted, research revealed no such catastrophic claims,[51] perhaps because of causation difficulties. But the parade of imagined horribles meant that the East Ohio Gas Company did not have to pay Mr. Stevenson $105.60, representing eight days of lost wages.[52] And concerns about asymmetrical remedies remained buried in law review articles and treatises.

One line of cases allowing recovery for pure economic loss did appear during this period, but it was quickly limited, serving only to highlight the resistance to unifying remedial standards for the consequences of negligent conduct. Negligent statements resulting in economic loss "only" became actionable as long as the claimant was the intended beneficiary, as compared to one of a general class of potential beneficiaries, of the statements. Two decisions by Justice Cardozo illustrate this point. In the 1922 case of *Glanzer v. Shepard*,[53] weighers under contract to the seller carelessly misrepresented the weight of beans to the buyer and were held liable for the amount overpaid by the buyer.[54] Cardozo found that the weighers, who, of course, had no contractual relationship with the buyer, nevertheless owed a duty of care to the buyer because "acting, not casually nor as mere servants, but in the pursuit of an independent calling [they] weighed and certified at the order of one with the very end and aim of shaping the conduct of

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50. *Id.* at 203–04.

51. *See id.* at 201.

52. *See id.* at 201, 204. Similarly, Justice Cardozo employed dire language in *Ultramares*, 174 N.E. at 444, a lawsuit that involved a single investor who repeatedly relied on negligent misrepresentations. *See supra* note 12 and *infra* note 58 and accompanying text.

53. 135 N.E. 275 (N.Y. 1922).

54. *See id.* at 275.

another."[55] By contrast, in *Ultramares Corp. v. Touche*,[56] decided in 1931, an accounting firm engaged to supply its client with an original plus thirty-two copies of a certified balance sheet was not liable for the losses of an investor who received and relied on one of the duplicates of the negligently prepared balance sheet.[57]

Glanzer may be distinguished from the general rule as a case in which the limit of liability was the value of the goods, as compared to the unknown number of persons who could claim reliance on the accounting firm's misrepresentation, the often quoted consideration being to avoid "liability in an indeterminate amount for an indeterminate time to an indeterminate class."[58] On the *Ultramares* facts, however, the claim of indeterminacy appears weak: The accounting firm delivered an original plus thirty-two copies; the plaintiff authorized repeated loans over a six to nine month period allegedly on the strength of the faulty financial statement; and no other similarly situated investors are identified in the opinion.[59] The limit of liability in *Ultramares* appears, therefore, both knowable and determinate.[60]

Glanzer may also be distinguished as a case in which the beneficiary of the service rendered was the third person, while in *Ultramares* the primary beneficary of the information was the corporation itself, not the lenders.[61] As Warren Seavey observes, however, this is a distinction without a difference:

> It is reasonably obvious that the weight card in the former case [*Glanzer*] was for the benefit of the seller as well as for the benefit of the buyer, and that in the latter case [*Ultramares*] the duplicate originals were intended for the benefit of third persons as well as for the client.[62]

Writing fifty years later, however, Robert Rabin asserts that *Glanzer* and *Ultramares* continue to demarcate the appropriate line

55. *Id.* at 277.

56. 174 N.E. 441 (N.Y. 1931).

57. *See id.* at 442.

58. *Id.* at 444. *But cf.* MacPherson v. Buick Motor Co., 111 N.E. 1050, 1053 (N.Y. 1916) (Cardozo, J.) (abandoning the privity doctrine).

59. *See Ultramares*, 174 N.E. at 442–43.

60. Cardozo did allow the claim of fraud to go forward in *Ultramares*. *See id.* at 447–49. It may be that Cardozo's invocation of an indeterminate class referred to an unexpressed fear that the class of potential investors relying on any accounting firm's certification might have greatly exceeded 32 persons, a reasonable fear in light of the extensive stock market activity preceding the 1929 crash.

61. *See* Warren A. Seavey, *Mr. Justice Cardozo and the Law of Torts*, 39 COLUM. L. REV. 20, 48 (1939).

62. *Id.* at 48.

between recoverable and unrecoverable stand-alone economic loss.[63] He reasons that the intended beneficiary criterion keeps liability to manageable levels, in the same way that the physical injury requirement appropriately circumscribes liability for consequential economic damages: In both types of cases the potential number of claimants has a "natural" limit.

This natural limit approach is vulnerable on two grounds. First, as we have seen, the early cases involve small, determinate claims whose particulars were less important than the general fear of unbounded liability arising from *any* expansion of tort doctrine.[64] Continued reliance on the specter of limitless recovery based on nothing but speculation betrays the rationale's poverty in an era of judicial opinions characterized by a commitment to logic, consistency, and context. Nor is financial exposure for physical harm as determinate as the theory of containing liability assumes. For example, there is simply no limit on potential damage awards for mass torts like improperly produced, tested, marketed, or implanted asbestos, cigarettes, silicon breast enhancers, or birth control devices.[65] These and other examples of liability involving indeterminate amounts for an indeterminate time to an indeterminate class are now familiar.[66] The proportionality concern that is one element of the issue of unbounded liability is similarly dated.[67] To take but two examples: "Mere" negligence now supports awards for mental distress suffered by the deceased before dying, as in

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63. *See* Rabin, *A Reassessment*, *supra* note 8, at 1527–28. *But cf.* Rabin, *Enterprise Liability*, *supra* note 18, at 1202–03 (recognizing that some courts go beyond the triangular relationship in allowing recovery for pure economic loss). The *Restatement (Second) of Torts* retains the requirement of intended beneficiary but extends liability to a known and intended *class* of beneficiaries. *See* RESTATEMENT (SECOND) OF TORTS § 552 (1977). The majority of jurisdictions follow *Ultramares*. *Cf.* Barber Lines A/S v. M/V Donau Maru, 764 F.2d 50, 55 (1st Cir. 1985). *But see* Peter Benson, *The Basis for Excluding Liability for Economic Loss in Tort Law*, *in* PHILOSOPHICAL FOUNDATIONS OF TORT LAW 427, 447 (David G. Owen ed., 1995) (claiming that the unstated but true distinction in these cases is between liability for misfeasance and nonliability for nonfeasance).

64. *See* Connecticut Mutual Life Ins. Co. v. New York & New Haven Ry., 25 Conn. 265 (1856), discussed *supra* notes 23–26 and accompanying text; *Byrd v. English*, 43 S.E. 419 (Ga. 1903), discussed *supra* notes 33–35 and accompanying text.

65. *See* Deborah R. Hensler & Mark A. Peterson, *Understanding Mass Personal Injury Litigation: A Socio-Legal Analysis*, 59 BROOK. L. REV. 961, 1040–42 (1993)(discussing the various damage awards and indicating that the possibility of receiving punitive awards has stimulated the surge in this type of lawsuit).

66. *Compare* Rabin, *A Reassessment*, *supra* note 8, at 1515 n.6 (suggesting that multiple claims from a wrongful course of conduct raise different issues than multiple claims from a single tortious act), *with* CANE, *supra* note 11, at 472–73 (disagreeing).

67. For a philosophical analysis of why disproportionate consequences are a part of the tort system, see Jeremy Waldron, *Moments of Carelessness and Massive Loss*, *in* PHILOSOPHICAL FOUNDATIONS OF TORT LAW, *supra* note 63, at 387.

Cook v. Ross Island Sand & Gravel Co.,[68] where the Court upheld an award of $35,000 for pain and suffering for the 2.5 minutes the deceased was alive before drowning;[69] and imposition of liability on social hosts for negligently inflicted injuries on third parties by drunk guests may not be considered disproportionate to the hosts' negligence in continuing to serve alcohol to those guests.[70] It may be, as James cautions, that the economies of the nineteenth and early twentieth centuries could not accommodate the magnitude of losses that are viewed as routine in the late twentieth century.[71] But whether the specter of financial ruin from recognizing modest, individual actions for economic loss was realistic or exaggerated at the time, that fear has little to tell us today about the reason for distinguishing economic from physical loss.[72]

Second, and of equal importance to understanding why the traditional story is misleading, tort doctrine is once again loosening the limits on recovery in various areas by reconfiguring the concepts of duty and causation, but stand-alone economic loss persists as a largely noncompensable harm.[73]

Perhaps the most dramatic recent change in tort doctrine is elimination of the "physical impact" rule, which held that persons frightened but not physically harmed by negligent conduct could not recover damages for resulting emotional distress, no matter how severe.[74] The long-standing "physical impact" requirement was explained as a way to insure the legitimacy of claims in fright cases

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68. 626 F.2d 746 (9th Cir. 1980).

69. *See id.* at 747–48; *see also* McAleer v. Smith, 791 F. Supp. 923 (D.R.I. 1992) (upholding claims for conscious pain and suffering before death by drowning); Capelouto v. Kaiser Found. Hosps., 500 P.2d 880, 885 (Cal. 1972) (finding that a jury may infer pain based on its common experience that pain accompanies the type of injury).

70. *See, e.g.*, Kelly v. Gwinnell, 476 A.2d 1219, 1220 (N.J. 1984).

71. *See* James, *supra* note 8, at 49. James attributes the failed campaign, in part, to the inherent correctness of limiting losses to manageable levels and the potential for stand-alone economic recovery to reach unacceptably high amounts. *See id.* at 47. For an illuminating discussion of contemporary strategies for dealing with liability, see Lynn M. LoPucki, *The Death of Liability*, 106 YALE L.J. 1, 14–38 (1996).

72. *Cf.* Koenig & Rustad, *supra* note 4, at 339–42 (discussing the use of million dollar punitive damage awards as a deterrent).

73. This may be another revolution in conceptualizing tort principles, but as with previous revolutions, the conceptual shift may prove more influential among legal commentators in law reviews than in case law. *See* Gary T. Schwartz, *The Beginning and the Possible End of the Rise of Modern American Tort Law*, 26 GA. L. REV. 601, 653–56 (1992) (tracing judicial disillusion with strict products liability). *Compare* RESTATEMENT (SECOND) OF TORTS § 402A (1965) (restating products liability in a single section), *with* RESTATEMENT (THIRD) OF TORTS: PRODUCTS LIABILITY (1998) (devoting an entire *Restatement* to products liability). The drafting process is described in David Owen, Essay, *Products Liability Law Restated*, 49 S.C. L. REV. 273, 278–287 (1998).

74. Emotional distress includes fright, grief, humiliation, and embarrassment. *See* RESTATEMENT (SECOND) OF TORTS § 46 cmt. j (1965).

and to limit the potential scope of liability.[75] On the other hand, once negligently caused physical impact was established, the plaintiff could recover for emotional distress (and economic loss) as parasitic damages; arguably the nature and extent of the physical injury would set appropriate boundaries for the claims of pain and suffering.[76] Responding to criticism that the impact rule arbitrarily singled out compensable from noncompensable injuries[77] and relying on contemporary understandings of psychic pain[78] and on greater faith in the medical judgment of mental health professionals,[79] beginning in 1968, most jurisdictions abandoned the physical impact requirement.[80] Thus, court decisions now talk about a duty to avoid creation of an unreasonable *risk* of physical harm, thereby allowing an independent tort for negligently caused emotional distress by persons frightened but not physically injured;[81] and judges

75. *See, e.g.*, Bosley v. Andrews, 142 A.2d 263, 266–67 (Pa. 1958) (describing the Pandora's box of false claims if the physical impact rule is eliminated). Justice Musmanno's colorful dissent is worth a look. *See id.* at 267–80 (Musmanno, J., dissenting).

76. *See id. But see* P.S. ATIYAH, ACCIDENTS, COMPENSATION AND THE LAW 213 (3rd ed. 1980) ("There appears to be simply no way of working out any relationship between the value of money—what it will buy—and damages awarded for pain and suffering, and disabilities."); Beagle v. Vasold, 417 P.2d 673, 681 (Cal. 1966) ("Every case which has considered the issue [of pain and suffering] . . . has emphasized the difficulty faced by a jury in attempting to measure in monetary terms compensation for injuries as subjective as pain. . . ."). It is estimated that over 60 percent of automobile liability payments in the United States are attributable to non-pecuniary damages. *See* Bruce Chapman & Michael J. Trebilcock, *Making Hard Social Choices: Lessons from the Auto Accident Compensation Debate*, 44 RUTGERS L. REV. 797, 815–16 (1992).

77. *See, e.g.*, Molien v. Kaiser Found. Hosps., 616 P.2d 813, 820 (Cal. 1980) (finding physical injury requirement overinclusive because it allows recovery even though physical injury is trivial and underinclusive because it denies plaintiffs an opportunity to prove the validity of a claim at trial).

78. *See* Peter A. Bell, *The Bell Tolls: Toward Full Tort Recovery for Psychic Injury*, 36 U. FLA. L. REV. 333, 402–03 (1984).

79. *See* Rodrigues v. State, 472 P.2d 509, 519–20 (Haw. 1970).

80. *See, e.g.*, Dillon v. Legg, 441 P.2d 912 (Cal. 1968) (providing standard authority for rejecting the physical impact requirement); Richard S. Miller, *The Scope of Liability for Negligent Infliction of Emotional Distress: Making "the Punishment Fit the Crime"*, 1 U. HAW. L. REV. 1, 3 (1979) (stating that the impact rule does not have widespread support). *But cf.* Metro-North Commuter R.R. Co. v. Buckley, 521 U.S. 424, 430, 439–40 (1997) (holding that a worker exposed to asbestos for three years on the job and who feared but had no physical sign of asbestos-related cancer could not maintain causes of action for negligent infliction of emotional distress or for future medical expenses under the Federal Employers' Liability Act (FELA)). For a state-by-state analysis of the physical impact requirement, see *Consolidated Rail Corp. v. Gottshall*, 512 U.S. 532, 544–49 (1994).

81. This is the "zone of danger" test. A good discussion of the policy reasons for limiting emotional distress claims to those within the zone of danger of physical injury can be found in *Gottshall*, 512 U.S. at 549–57. The *Gottshall* court adopted the zone of danger test for FELA and expressly rejected a broader standard that would have permitted recovery for negligently inflicted emotional distress when, in the words of the Court of Appeals below, "the factual circumstances . . . provide a threshold assurance that there is a likelihood of genuine and serious emotional injury." Gottshall v. Consolidated Rail Corp., 988 F.2d 355,

regard bystanders who suffer emotional distress from witnessing negligent injury to a loved one as "foreseeable plaintiffs."[82] To narrow the classes of direct and bystander parties who may sue for emotional distress, courts impose evidentiary requirements such as severe psychic trauma,[83] contemporaneous observation of the negligent act and its consequences,[84] an intimate family relation between the physically and the emotionally injured parties,[85] or a pre-existing contractual or fiduciary relationship between patient and physician.[86] As with the abandonment of privity and the adoption of strict liability for harm caused by defective products, a mechanical no recovery rule has changed in just over ten years[87] to a system in which changing conceptions of duty and causation do the work of limiting liability.[88]

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371 (3d Cir. 1993); *see also Metro-North*, 521 U.S. at 430–32 (no FELA claim for on-the-job exposure to asbestos in the absence of a physical manifestation of illness).

82. Dillon v. Legg, 441 P.2d 912, 921 (Cal. 1968) (holding that a mother who witnessed death of infant by negligent motorist may state a claim for emotional distress even though she was not physically at risk).

83. *See Rodrigues*, 472 P.2d at 520 (finding that concerns about the genuineness of claims and unlimited liability could be addressed by a jury applying the standard of severe or serious mental distress and through the application of tort law's general principle of foreseeability).

84. *See Dillon*, 441 P.2d at 921.

85. Jurisdictions differ as to whether the negligent conduct must be directed toward a member of one's nuclear family and whether contemporaneous observation of the conduct, of the accident, and of its physical consequences are required. *See* J. Mark Appleberry, *Negligent Infliction of Emotional Distress: A Focus on Relationships*, 21 AM. J.L. & MED. 301, 309–312 (1995) (summarizing recent cases).

86. *See, e.g.*, Chizmar v. Mackie, 896 P.2d 196, 205 (Alaska 1995) (holding that emotional distress resulting from a misdiagnosis of AIDS is foreseeable and serious). Emotional distress from harm to real or personal property may also be recoverable. *See* Bode v. Pan Am. World Airways, Inc., 786 F.2d 669, 672 (5th Cir. 1986) (damage resulting from an airline crash); *Rodrigues*, 472 P.2d at 520 (flood damage to home); Moorehead v. State Dep't of Highways, 353 So. 2d 1103, 1105 (La. Ct. App. 1977) (removal of trees and exposure of roots on residential lawn). *But see* HAW. REV. STAT. ANN. § 663-8.9 (Michie 1995) (restricting plaintiffs suing for emotional distress arising from damage to property to prove attendant physical injury or mental illness); *cf.* Zeigler v. F St. Corp., 235 A.2d 703, 705 (Md. 1967) (allowing no recovery for mental distress resulting from flooding of land); Buchanan v. Stout, 108 N.Y.S. 38, 39 (1908) (finding no recovery for mental distress resulting from the death of the plaintiff's cat).

87. *See* Miller, *supra* note 80, at 3.

88. Other areas in which traditional limitations on duty have been relaxed include a therapist's failure to warn an identified victim of death threats communicated by the therapist's patient, *see* Tarasoff v. Regents of Univ. of Cal., 551 P.2d 334, 353 (Cal. 1976); Rabin, *Enterprise Liability*, *supra* note 8, at 1200 n.64, and employment-related injury from negligent misrepresentations or negligent infliction of emotional distress, *see infra* text accompanying notes 89–94. *But see* Leslie Benton Sandor & Carol Berry, *Recovery for Negligent Infliction of Emotional Distress Attendant to Economic Loss: A Reassessment*, 37 ARIZ. L. REV. 1247, 1269–77 (1995) (criticizing courts for refusing emotional distress damages attendant on pure economic loss).

In an equally dramatic decision, the Montana Supreme Court recently abolished the distinction between negligent and intentional infliction of emotional distress, establishing infliction of emotional distress as a single, independent cause of action.[89] Generally, in the tort of intentional infliction of emotional distress, the plaintiff is required to establish the outrageousness of the defendant's behavior, presumably to guard against specious claims of crippling emotional distress arising from merely nasty conduct.[90] But, as the Montana court pointed out, there were no reported cases in which a plaintiff had prevailed on a claim of intentional infliction of emotional distress,[91] suggesting that the gate-keeping function of the outrageousness element may have turned into a claim-barring device. To address concerns about a floodgate of claims and unlimited liability, the court chose to rely on the plaintiff's obligation to prove serious or severe emotional distress and stated that such distress was a "reasonably foreseeable consequence of the defendant's negligent act or omission."[92] Although the dispute in *Sacco v. High Country Independent Press, Inc.*[93] arose over the defendants' comments and actions after the plaintiff left their employment, the court explicitly identified personal, property, and legal interests as covered by the new cause of action when conduct results in severe or serious emotional distress.[94]

In both the fright and distress causes of action, negligent conduct inflicts an emotional, not physical,[95] harm, but the

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In a related development, Rabin observes the "more robust principle of fault" in medical malpractice cases, noting abandonment of the same locality rule, expansive use of res ipsa loquitur, less restrictive standards for qualifying experts, and ease in establishing the absence of informed consent. *See* Rabin, *Enterprise Liability*, *supra* note 8, at 1200–01.

In environmental disputes, damages for the loss of nature may be added to commercial losses. *See generally* Alan Strudler, *Valuing Nature: Assessing Damages for Oil Spills*, REP. FROM INST. FOR PHIL. & PUB. POL'Y, Winter 1995, at 6.

89. *See* Sacco v. High Country Indep. Press, Inc., 896 P.2d 411, 427–29 (Mont. 1995).

90. *See* Regina Austin, *Employer Abuse, Worker Resistance, and the Tort of Intentional Infliction of Emotional Distress*, 41 STAN. L. REV. 1, 6, 15–18 (1988) (discussing cases and RESTATEMENT (SECOND) OF TORTS § 46 (1965)).

91. *See Sacco*, 896 P.2d at 427. The failure to discover successful causes of action in economic loss cases often leads to the opposite conclusion, *viz.* that the categorical refusal is sensible. *See, e.g.*, Stevenson v. East Ohio Gas Co., 73 N.E.2d 200 (Ohio 1946), discussed *supra* notes 47–52 and accompanying text; James, *supra* note 8.

92. *Sacco*, 896 P.2d at 425.

93. 896 P.2d 411 (Mont. 1995). The Montana Court relied heavily on the reasoning in the Hawaii Supreme Court's opinion in *Rodrigues v. State*, 472 P.2d 509, 518–21 (Haw. 1970).

94. The definition of severe or serious emotional distress is found in RESTATEMENT (SECOND) OF TORTS § 46 cmt. j (1965). The Supreme Court of Montana reaffirmed *Sacco* in *Treichel v. State Farm Mutual Auto Insurance Co.*, 930 P.2d 661, 665 (Mont. 1997).

95. Unlike the Montana Supreme Court, most courts faced with wrongful discharge lawsuits alleging negligent misrepresentation or negligent infliction of emotional distress

consequences experienced by the plaintiffs are sufficiently similar to those resulting from physical injury to justify a remedy, and contemporary courts expect notions of duty and causation to rein in tendencies towards frivolous claims or ruinous liability. In contrast, when it comes to stand-alone economic injury, most courts and commentators cling to the rhetoric of preventing widespread liability and affirm the reasonableness of a general bar to recovery; among others, James and Rabin insist that the concern about widespread liability is empirically[96] and morally[97] sound. Part II challenges this orthodoxy by using contemporary notions of duty and causation to analyze claims of pure economic loss.

II.

A favorite illustration of the need to limit liability by not compensating pure economic injury is Judge Kaufman's 1968 hypothetical of the unlucky motorist whose inadvertence causes an accident that shuts down the Brooklyn Battery Tunnel during rush hour:[98]

> A driver who negligently caused such an accident would certainly be held accountable to those physically injured in the crash. But we doubt that damages would be recoverable against the negligent driver in favor of truckers or contract carriers who suffered provable losses because of the delay or to the wage earner who was forced to "clock in" an hour late. And yet it was surely foreseeable that among the many

fail to address the doctrinal limits on recovery for emotional harm unaccompanied by contemporaneous physical injury. *See, e.g.*, Austin, *supra* note 90, at 8–12 (discussing traditional employment cases). The courts struggle with whether to recognize a right for negligent misrepresentation or distress in the employment context, seemingly oblivious to the fact that the remedy for such a violation involves the traditionally rejected award of damages for economic loss "only." *See id.*

96. *See* James, *supra* note 8, at 51.

97. *See* Rabin, *A Reassessment*, *supra* note 8, at 1534 (asserting that proportionality is a consistent feature of the tort system). *But see* CANE, *supra* note 11, at 473 (asserting that in tort, there are no degrees of legal fault); Waldron, *supra* note 67 (comparing the potential liability of equally negligent actors, only one of whom causes a harm).

98. *See* Kinsman Transit Co. v. City of Buffalo, 388 F.2d 821, 825 n.8 (2d Cir. 1968) (*Kinsman II*).

[thousands] who would be delayed would be truckers and wage earners.[99]

Many readers may find themselves mentally nodding in agreement with Judge Kaufman. As described, liability to thousands, none of whom suffered physical injury, for mere inadvertence may look disproportionate, perhaps ruinous. But let us investigate this intuitive response. First, as compared to awards for pain and suffering, the loss from economic injury is provable, not subjective or speculative.[100] And even if delay costs 3000 motorists an average of $500 each (a generous assumption), the negligent driver's liability looks to be about $1.5 million, a significant sum, but hardly pauperizing in a world of multi-million dollar awards to one or two parties seriously injured in traffic accidents.[101] Also noteworthy is the grouping of truckers and contract carriers with wage earners as equally undeserving claimants. The truckers and contract carriers are likely to be insured against losses occasioned by delays, whereas wage earners will not be. Perhaps eligibility for economic loss should exclude professional drivers and carriers in the course of their business, just as public safety officials cannot recover for negligently caused physical harm incurred while performing their jobs.[102] But why exempt the wage-earners?[103] Even more curious is the absence of any specific reference in the hypothetical to liability

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99. *Id.* Positive references can be found in *Barber Lines A/S v. M/V Donau Maru*, 764 F.2d 50, 52 (1st Cir. 1985), and Rabin, *A Reassessment*, *supra* note 8, at 1525 n.39, 1536 n.73. *See also* KENNETH S. ABRAHAM, THE FORMS AND FUNCTIONS OF TORT LAW 234 (1997) ("The reason [there is very little deviation away from the rule denying recovery for pure economic injury] is that the considerations that supported the rule a century ago still largely support it."); JOSEPH W. GLANNON, THE LAW OF TORTS: EXAMPLES AND EXPLANATIONS 155 (1995) ("[I]t is clear that liability is denied because of the burden such losses would impose, *not* because secondary economic losses are unforeseeable."); Schwartz, *supra* note 46, at 59 n.120 (explaining that only the product owner will be harmed by economic loss because any other party suffering economic loss may be "tantamount to a bystander" and unable to recover the loss).

100. For an examination of the disparity between awards for physical injury and consequential damages, see Randall R. Bovbjerg et al., *Valuing Life and Limb in Tort: Scheduling "Pain and Suffering"*, 83 NW. U. L. REV. 908 (1989).

101. *See* Hensler & Peterson, *supra* note 65, at 1040–42.

102. *See, e.g.*, Zanghi v. Niagara Frontier Transp. Comm'n, 649 N.E.2d 1167, 1170 (N.Y. 1995) (holding police and fire fighters barred from recovery where performance of duty increased the risk of injury).

103. Even if one of the wage earners is a highly compensated executive whose damages far exceed the hypothetical average, this should make no difference to the analysis. Tort doctrine generally requires the defendant to take her victim as she finds her for purposes of measuring damages after liability has been established. *See* Steinhauser v. Hertz Corp., 421 F.2d 1169, 1172 (2d Cir. 1970). Once again, a comparison to consequential economic loss is apt: breaking the arm of a concert violinist and breaking the arm of a retired librarian each trigger liability, although for vastly different sums of money.

for property damage occasioned by the accident, the appropriately compensated being "those physically injured." Certainly the car owner whose automobile, though not involved in the primary accident, suffers $5000 damages attributable to the negligently caused crash will receive compensation for repairs and consequent economic harm. Similarly, if the negligent motorist caused minor physical damage to 3000 vehicles, delaying each driver an hour, in principle all drivers could recover for their proven economic losses as consequential damages from injury to their property.[104] Why should the fortuity of minor harm to property entitle these drivers to recover for economic loss? And what if two tennis stars on their way to compete in the United States Open are involved in this auto accident, one athlete suffering a minor wrist sprain while the other endures only a delay that results in a forfeited match? For both tennis players, the consequences that matter are identical; athletes with a chance at titles are denied a singular opportunity to prove themselves, losing rankings, prize money, and endorsements. But only the athlete with the sprained wrist has a compensable injury and the opportunity to claim consequential economic damages.

On the other hand, viewed through the lens of pragmatism, how likely is it that many wage earners docked one hour's pay (or a class of wage earners) will engage lawyers to recover the lost earnings from the negligent driver? When the unusual claim for pure economic loss occurs, ought not the courts face the question of when "the link has become too tenuous—that what is claimed to be consequence is only fortuity"?[105] And the hypothetical ignores third-party insurance and the benefit of spreading the risk among

104. The absence of any reference to property damage in the hypothetical is even more startling when one compares Kaufman's observation in note seven of the opinion that "where there is physical damage to a vessel the owner can recover for the loss of its use until repairs are completed." *Kinsman II*, 388 F.2d at 825 n.7. Perhaps Judge Kaufman's silence on the right to damages for harm to property reflects his unexpressed recognition that property damage is, in effect, economic loss. *See infra* notes 153–60 and accompanying text.

105. *Kinsman II*, 388 F.2d at 825. Judge Kaufman refuses to use the negligent interference with contract doctrine upon which the district court relied and instead opts for "more familiar tort terrain," *id.* at 824, that is, "the circumlocution whether posed in terms of 'forseeability,' 'duty,' 'proximate cause,' 'remoteness,' etc . . . ." *Id.* at 825. It is one of the ironies of this opinion that, in analyzing the case under this "more familiar tort terrain," Kaufman explicitly rejects the proportionality and floodgates arguments as reasons for relying instead on interference with contract. *See id.* at 823–24.

According to Judge Kaufman, "Here, as elsewhere, the answer must be that courts have some expertise in performing their almost daily task of distinguishing the honest from the collusive or fraudulent claim. And, 'if the result is out of all proportion to the defendant's fault, it can be no less out of proportion to the plaintiff's entire innocence.'" *Id.* at 823 (quoting WILLIAM PROSSER, HANDBOOK OF THE LAW OF TORTS 964 (3d ed. 1964)). Of course, Kaufman then poses the widely-cited hypothetical under discussion in note eight of the opinion. *See id.* at 825 n.8; discussion *supra* note 99.

motorists, any one of whom could be the careless injurer or the unlucky injured.[106] Thus, on close analysis the intuitive appeal of categorical denial of recovery for pure economic loss in order to forestall unacceptably widespread liability disappears. There may be instances of potentially ruinous liability but those instances do not serve as the foundation for the general rule prohibiting recovery for economic loss.

Let us imagine for a moment a highly improbable legal regime in which the question of liability in tort for causing pure economic injury had never been addressed or even hypothesized; but the tunnel accident imagined by Judge Kaufman occurs, and claims for pure economic loss arise in a case of first impression. The tort of negligence is commonly said to have four elements: (1) unreasonable conduct, (2) causation, (3) duty, and (4) harm. In the tunnel accident, the negligent driving caused an accident, resulting in physical injury to some but in delay without physical harm to thousands of others. And Judge Kaufman concedes that the plaintiffs, the economic harm, and the delay are foreseeable. Thus, the outstanding question appears to be whether the negligent driver owed a duty to the thousands of persons delayed and economically injured. On what sources would a court rely in determining the question of duty? We have stipulated that there are no precedents directly on point, but perhaps guidance will be found in discussions from recent case law, the *Restatement (Second) of Torts*, treatises, or law reviews.

As every first-year law student learns, the question of whether a relation exists between individuals which imposes upon one a legal obligation for the benefit of the other is not capable of being answered in the abstract.[107] Prosser tells us that "as our ideas of human relations change the law as to duties changes with them" and that "[n]o better general statement can be made than that the courts will find a duty where, in general, reasonable persons would recognize it and agree that it exists."[108] But he goes on to identify factors commonly used by courts in finding a duty:

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106. Curiously, when insurance is considered, authors indulge in inconsistent assumptions about the identity and insurance practices of various parties, often, it seems, to assert the likelihood of spreading risks and costs appropriately. *See, e.g.*, J.A. Smillie, *Negligence and Economic Loss*, 32 U. TORONTO L.J. 231, 237–39 (1982). *But see* CANE, *supra* note 11, at 502 (criticizing Smillie). On the role of insurance in general in tort cases involving economic interests, see *id.* at 431–61.

107. *See generally* KEETON ET AL., *supra* note 18, § 53.

108. *Id.* § 53, at 359.

(1) the foreseeability of harm to the plaintiff,
(2) the degree of certainty that the plaintiff was harmed,
(3) the closeness of the connection between defendant's conduct and plaintiff's harm,
(4) the extent of moral blame attached to the defendant's conduct,
(5) the policy of preventing future harm,
(6) the burden on the defendant and impact on the community of imposing a duty, and
(7) the availability, cost and prevalence of insurance for the risk involved.[109]

Not surprisingly, we have already established some of these factors in the preceding paragraph: (1) Foreseeability: automobile accidents during heavy traffic cause injury to persons and property and delay for many drivers; (2) Certainty of Harm: the economic consequences of delay are readily ascertainable and verifiable; and (3) Causation: in the hypothetical there is no question that the negligent conduct is responsible for the delays and there are no intervening events. It is difficult to assess the role of (4) Moral Blameworthiness in our analysis of duty. Arguably, once we have identified the negligent act or omission, the inquiry into moral blameworthiness is over. Indeed, as Peter Cane has noted:

> [V]ery large amounts of damages can be payable for personal injuries *and property damage* as a result of disasters such as explosions in chemical factories or on marine oil platforms; but no one suggests that the damages payable should be limited because they might be out of proportion to the degree of fault involved. On the contrary, the degree of (moral) fault seems to be judged according to the size of the injury inflicted, regardless of the nature of the tortious conduct.[110]

Yet some commentators continue to insist that proportionality must limit liability in the context of economic losses.[111] Perhaps the degree of moral blameworthiness adds weight when the other factors point decidedly in one direction but do not alter the calculation. Deterrence, (5) and (6), is as malleable a concept as

109. *Id.* § 53, at 359 n.24.

110. CANE, *supra* note 11, at 473 (emphasis in original).

111. *See* Rabin, *A Reassessment*, *supra* note 8, at 1534–36; Rabin, *Enterprise Liability*, *supra* note 18, at 1202–03.

moral blameworthiness. We can say, on the one hand, that full realization of the scope of potential damages will reinforce one's desire to drive carefully; on the other hand, negligence is by definition inadvertence and one victim with an eggshell skull may experience far more significant damage than thousands of victims with minor injuries. The deterrence calculation might also take into account the cost and annoyance associated with filing and litigating a legal claim; careless drivers might gamble that only those with a very large (pure) economic loss will bother to make a claim and that such claimants are rare. The inquiry regarding the availability and effect of (7) Insurance is largely a canard.[112] Insurance coverage follows liability rules,[113] and a rule making pure economic loss recoverable in tort could easily be accommodated through third- or first-party insurance.[114] It is, therefore, very much an open question whether a court faced with the tunnel accident as a case of first impression in 1999 would hold the negligent driver to have a duty to those suffering pure economic loss.

The reasonableness of the concern about unknowable, catastrophic liability and the fairness of the no recovery rule can be further tested by looking at the few cases in which courts have rejected the categorical prohibition and subjected recovery for pure economic loss to the reconfigured concepts of duty and causation that are broadening liability elsewhere.

The New Jersey Supreme Court undertook a thorough consideration of duty and causation in *H. Rosenblum, Inc. v. Adler*,[115] a 1983 case which once again raised the question of auditors' liability for the financial losses of third parties. Rejecting the *Ultramares* restriction of liability to intended beneficiaries only and the *Restatement's* limitation to a known and intended class of beneficiaries, the court held auditors liable to persons whom the auditors should reasonably have foreseen would be given and would rely upon the audit.[116] The court noted the expertise and independence of professional accountants who perform audits[117] and tort law's repudiation of privity.[118] More importantly, however,

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112. *See* CANE, *supra* note 11, at 445–46.

113. *See* Kelly v. Gwinnell, 476 A.2d 1219, 1225 (N.J. 1984) (observing that homeowners' insurance policies will cover host liability for drunken guests' subsequent negligent auto accident).

114. *See* LoPucki, *supra* note 71, at 72–75 (describing insurance instruments).

115. 461 A.2d 138 (N.J. 1983).

116. *See id.* at 153.

117. *See id.* at 150.

118. *See id.* at 145–46. The New Jersey Court relied, in part, on an earlier decision holding manufacturers liable for economic losses occasioned in connection with products liability. *See* Santor v. A. & M. Karagheusian, 207 A.2d 305, 310–11(N.J. 1965). The court

the court discredited the reasonableness of "the spectre of financial catastrophe"[119] by examining the liability question in light of developments outside and within tort law. Thus, the court pointed out that purchasers of securities in public offerings already have a claim against accounting firms for misstatement of a material fact in financial statements;[120] that independent auditors have been able to obtain liability insurance covering these risks and that there is no reason to believe they could not purchase malpractice insurance to cover negligent acts leading to detrimental reliance by persons who receive the audit from a company pursuant to a proper business purpose;[121] that imposition of a duty may promote more careful reviews, arguably leading to fewer mistakes;[122] that the costs of increased diligence will be borne by the insurer or its customers;[123] that the extent of financial exposure has built-in limits, because it applies "only to those foreseeable users who receive the audited statements from the business entity for a proper business purpose to influence a business decision of the user, the audit having been made for that business entity;"[124] and that damages would be limited to actual losses from reliance on the misstatement.[125]

Extending the foreseeability analysis beyond the professional malpractice configuration,[126] the same court, in *People Express Airlines v. Consolidated Rail*,[127] allowed a cause of action for economic

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subsequently ruled that a commercial buyer could not sue in products liability for economic losses, distinguishing *Santor* as a case involving an ordinary consumer. *See* Spring Motors Distrib., Inc. v. Ford Motor Co., 489 A.2d 660, 670 (N.J. 1985). In reconsidering its position on responsibility for economic losses in connection with products liability, the New Jersey Supreme Court noted the rejection of *Santor* by most other state courts. *See id.* at 669–70. The court's discussion in *Rosenblum* of the inadequacies of the widespread liability theory are in no way dependent on the adoption of *Santor* and survive its reformulation in *Spring Motors*.

119. *Rosenblum*, 461 A.2d at 151.

120. *See id.* (citing the Securities Act of 1933, 15 U.S.C. § 77k, and the Securities Exchange Act of 1934, 15 U.S.C. § 78r).

121. *See id.* at 151.

122. *See id.* at 152.

123. *See id.*

124. *Id.* at 153.

125. *See id.* at 152. *But cf.* Credit Alliance Corp. v. Arthur Andersen & Co., 65 N.Y.2d 536, 551 (1986) (rejecting *Rosenblum*).

126. *Cf.* Rabin, *Enterprise Liability*, *supra* note 18.

127. 495 A.2d 107 (N.J. 1985). *Accord* Mattingly v. Sheldon Jackson College, 743 P.2d 356, 360 (Alaska 1987) (adopting particular foreseeability analysis in claim for loss of income and profits as a result of negligently caused loss of employee services). *But see* Barber Lines A/S v. M/V Donau Maru, 764 F.2d 50, 56–57 (1st Cir. 1985) (declining to depart from the no recovery rule on the grounds of precedent and policy); Louisiana *ex rel.* Guste v. M/V Testbank, 752 F.2d 1019, 1028–29 (5th Cir. 1985) (same); Dundee Cement Co. v. Chemical Labs., Inc., 712 F.2d 1166, 1170–72 (7th Cir. 1983) (same, applying Illinois law); Leadfree Enters. v. United States Steel Corp., 711 F.2d 805, 807 (7th Cir. 1983) (same, applying Wisconsin law); FMR Corp. v. Boston Edison Co., 613 N.E.2d 902, 903–04 (Mass.

loss by an airline forced to evacuate its terminal when a chemical was negligently released from a railroad tank car located less than a mile away.[128] The court was explicit about its new approach to cases of pure economic loss:

> Whatever the original common law justifications for the physical harm rule, contemporary tort and negligence doctrine allow—indeed, impel—a more thorough consideration and searching analysis of underlying policies to determine whether a particular defendant may be liable for a plaintiff's economic losses despite the absence of any attendant physical harm.[129]

The court was careful to require particular foreseeability: "[D]efendant's capacity to have foreseen . . . the particular plaintiff or identifiable class of plaintiffs . . . is demonstrably within the risk created by defendant's negligence."[130] Thus, the airline's lost revenue could be recovered on a showing that the defendants knew of the danger presented by escaped chemicals and had in place a plan of evacuation should an accident occur.[131] But those inquiring about future flights could not claim damages, for example, for lost earnings attributable to the evacuation.[132] *Rosenblum* and *People Express* look like conceptual cousins of the cases extending liability for fright and distress.[133]

1993) (same); United Textile Workers of Am. v. Lear Siegler Seating Corp., 825 S.W.2d 83, 86 (Tenn. Ct. App. 1990) (disapproving expressly *People Express*).

128. *See People Express*, 495 A.2d at 109.

129. *Id.* at 111.

130. *Id.* at 118; *see also id.* at 116 ("The more particular is the foreseeability that economic loss will be suffered by the plaintiff as a result of defendant's negligence, the more just is it that liability be imposed and recovery allowed.").

131. *See id.* at 118.

132. The New Jersey court appears sensitive to the indeterminacy of the particular forseeability formulation: "[S]ome cases will present circumstances that defy the categorization here devised . . . . In these cases, the courts will be required to draw upon notions of fairness, common sense and morality to fix the line limiting liability as a matter of public policy, rather than an uncritical application of the principle of particular forseeability." *Id.* at 116.

133. Lord Devlin's observation in *Hedley Byrne & Co. v. Heller & Partners*, [1964] App. Cas. 465 (H.L.), is instructive:

> The interposition of the physical injury is said to make a difference of principle. I can find neither logic nor common sense in this. . . . [I] think this to be nonsense. It is not the sort of nonsense that can arise even in the best system of law out of the need to draw nice distinctions between borderline cases. It arises, if it is the law, simply out of a refusal to make sense.

Similarly, in *Pruitt v. Allied Chemical Corp.*,[134] a federal district court looked at the purposes of tort law, rather than strong precedent against liability for pure economic loss, to allow negligence actions by some parties alleging financial injury from the polluting of Chesapeake Bay. The plaintiffs included the bay's commercial fishermen, distributors of bay produce, businesses that serviced the bay's sportsfishing interests, and the employees of all three groups.[135] In deciding which categories of plaintiffs could proceed against Allied Chemical, Judge Mehrige candidly observed: "[T]he set of potential plaintiffs seems almost infinite ... [S]ome limitation to liability [for economic losses], even when damages are foreseeable, is advisable.... The Court thus finds itself... without any articulable reason for excluding any particular set of plaintiffs."[136] Nonetheless, the court proceeded to classify plaintiffs according to familiar tort criteria.[137] Beginning with the defendants' concession of commercial fishermen's right to proceed, Judge Mehrige reasoned that sportsfishermen had as direct a "constructive property interest in the Bay's harvestable species" as the commercial fishermen.[138] Then, in recognition of each sportsfisherman's limited economic incentive to litigate, the court also allowed businesses that alleged lost profits to sue as "surrogate[s]" for the sportsfishermen.[139] With regard to the distributors of bay produce and their employees, however, the court concluded that, though undeniably and foreseeably injured by the alleged pollution, their claims were not cognizable because they were

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Id. at 517. *Hedley Byrne*, the British treatment of pure economic recovery from negligent conduct, and the "capricious" results are analyzed in Atiyah, *supra* note 8, at 256–65. *See also* Strauss v. Belle Realty Co., 482 N.E.2d 34, 38–41 (N.Y. 1985) (Meyer, J., dissenting) (criticizing the majority's unexamined acceptance of Con Edison's claim of potentially crushing liability from a mass electrical blackout).

134. 523 F. Supp. 975 (E.D. Va. 1981).

135. *See id.* at 976 n.1.

136. *Id.* at 979–80 (footnote omitted).

137. The Court of Appeals for the Fifth Circuit expressly declined, Judge Wisdom dissenting, to abandon the no recovery rule in another oil spill case, rejecting the use of foreseeability analysis. *See* Louisiana *ex rel.* Guste v. M/V Testbank, 752 F.2d 1019, 1028–29 (5th Cir. 1985); *see also* Barber Lines A/S v. M/V Donau Maru, 764 F.2d 50, 52–53 (1st Cir. 1985) (discussing *Guste* with approval).

138. *Pruitt*, 523 F. Supp. at 978. The defendants' concession of liability to the commercial fishermen may have been prompted by their recognition that commercial fishermen are special "favorites of admiralty." Union Oil Co. v. Oppen, 501 F.2d 558, 567 (9th Cir. 1974) (commercial fishermen allowed lost profits from large oil spill that killed fish). *But see* Rabin, *A Reassessment*, *supra* note 8, at 1535 n.72 (dismissing *Oppen* as of "virtually no general interest as a dispute over economic loss ... [because it] involved the definition of property rights in a commons, a question entirely distinct from the issues raised in most economic loss cases").

139. *See Pruitt*, 523 F. Supp. at 980.

"insufficiently direct."[140] In essence, Judge Mehrige populates the familiar categories of "directly" and "indirectly" harmed plaintiffs so that infinite liability is avoided but "[d]estruction of the Bay's wildlife . . . [is not] a costless activity."[141]

These rare examples show the power of tort law's general principles to do the work of separating compensable from noncompensable economic losses. Unlike other recent examples of expanded recovery, however, utilization by a few courts of contemporary notions of duty and causation in the context of claims for economic loss has not stimulated other jurisdictions to follow.[142] The question is why the vast majority of courts persist in the categorical denial of recovery for pure economic loss.[143]

III.

If, as I have suggested, the reasons advanced for excluding pure economic loss from the category of recoverable injuries are largely unpersuasive, am I able to offer another, more plausible account? The proposition that I want to essay is this: The categorical refusal to award damages for economic loss "only" obscures some hard questions posed by capitalist economic arrangements, and it enjoys ready acceptance because ideology, tradition, and perspective combine to keep us from even imagining those questions.

As already noted, negligently inflicted pure economic losses bear a striking similarity to losses in routine market transactions. Recall the example of the two investors who lose millions of dollars, one due to a company's poor business judgment and the

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140. *Id.*

141. *Id.* at 978. The court was also concerned that the defendants pay only once for the alleged pollution and believed that the line it drew between plaintiffs and nonplaintiffs accomplished that purpose. *Id.* at 979. McThenia and Ulrich criticize the distinction between the lost economic interests of businesses and distributors dependent on an unpolluted Chesapeake Bay, note that the precedents supported dismissal of the claims of both categories of plaintiffs, speculate that Judge Mehrige used the motion to dismiss to try to force a settlement, and describe the decision to allow the surrogates to maintain a cause of action in negligence as "imaginative." *See* Andrew W. McThenia & Joseph E. Ulrich, *A Return to Principles of Corrective Justice in Deciding Economic Loss Cases*, 69 VA. L. REV. 1517, 1529–34 (1983).

142. *See supra* note 137.

143. The refusal is even more striking in light of the limitations on liability being put into place by legislation and insurance companies. *See* LoPucki, *supra* note 71, at 69–70. Similarly, where socially desirable behavior is likely to cause grievous harm in the event of an accident, legislation in selected areas seeks to balance the cost to the injured and the injuror. *See* Price-Anderson Act, 42 U.S.C. § 2210 (1994) (limiting an operator's total liability for a nuclear accident).

other due to a poorly maintained utility transformer. In both instances, the investors relied to their detriment on the exercise of reasonable care by parties with superior knowledge and ability who nonetheless made mistakes. If the investor harmed by a faulty communications line could recover the pure economic loss, it is difficult to explain why the investor harmed by the faulty business decisions could not similarly claim damages. By making recovery of economic loss in tort dependent on physical injury, the nature of risk in the marketplace is obscured.

Softening the rough edges of capitalism by truncating inquiry is common, often so common as to escape notice. In a challenging article, Lynn LoPucki describes the many devices by which businesses lawfully avoid liability and the ideology that supports them.[144] The following is a gross simplification of just one of his examples: In asset securitization, a company's asset-holding and liability-generating components are separated into two free-standing companies, in the name of maximizing earning potential and stock value. In the event of a successful claim against the liability-generating company, however, that company is judgment proof and is also treated as legally unrelated to the asset-holding company. This structuring of financial relations, which LoPucki designates the "silver bullet capable of killing liability,"[145] is legal, apparently.[146] And, as LoPucki notes, "when the assets and insurance of a large, publicly held company are insufficient to pay its liabilities, most commentators still consider it the result of financial reversals rather than of strategic preparation for the possibility of financial reversals."[147] Indeed, LoPucki reminds us that corporate bankruptcy went from being a stigmatizing event in 1980 to " 'an acceptable, trendy reorganizing tool' "[148] by the early 1990s, and asks, "[c]ould Americans come to see the judgment proofing of the largest companies in the same way?"[149] His answer merits extended quotation:

> To be culturally and politically acceptable, the process of judgment proofing must appear to be something other than what it is. There is every reason to believe that it will. . . . The

144. *See* LoPucki, *supra* note 71, at 14–38. For a colloquy on LoPucki's observations, see James J. White, *Corporate Judgment Proofing: A Response to Lynn LoPucki's* The Death of Liability, 107 YALE L.J. 1363 (1998), and Lynn M. LoPucki, *Virtual Judgment Proofing: A Rejoinder*, 107 YALE L.J. 1413 (1998).

145. LoPucki, *supra* note 71, at 30.

146. *See id.* at 24–30.

147. *Id.* at 53–54.

148. *Id.* at 44 (citation omitted).

149. *Id.* at 53.

public image of asset securitization is that of the invisible hand of the market, aided by modern technology, generating wealth by forging increasingly sophisticated financial structures. Eventually it will become obvious that the invisible hand is not an efficient allocator of resources, because it is moved only by the interests of *contract* creditors. But so long as the companies march into this new world in tandem, each objecting that it is forced into its course of action by competitive pressures, it will be difficult for indignation to take hold.* The problem will be seen, not entirely incorrectly, as systemic rather than moral.

* This is essentially the formulation successfully employed by many of the same companies during the 1980s when they were criticized for actions that reduced their labor costs.[150]

Immunizing economic loss from recovery in tort law shares the chameleon quality LoPucki describes. The image is of noncontractual economic loss as ruinous liability threatening the financial stability of business, industry, and insurance; this catastrophic picture, if reproduced often enough, becomes fixed, seemingly universal, and inevitable.[151] Missing from this image is the reality that the major players in this game *could* protect themselves from ruinous liability through contract, that they choose instead to present themselves as unable to do so, and that they then cite the consequences of their choice as the reason the law should not allow recovery for an acknowledged injury.

In addition to ideology, another reason it is easy to ignore the anomaly of the economic loss doctrine is the traditional division of civil claims into those which arise from breaches of contract and those which occur in the absence of a contract. Contract addresses consensual economic expectations and their failure; tort focuses on allocating the costs from noncontractual injury to persons and property. Understandably, judges and commentators who rope off pure economic loss from compensation routinely examine the tort system using the touchstone of physical injury to persons and property, even though the measure of damages depends significantly on consequential losses, including economic ones. Indeed, as the law

150. *Id.* at 54 (emphasis in original).

151. After exhaustive review of the literature, Galanter finds little evidence for the sustained insistence that remedying injuries to persons and property burdens the country's economic well-being, particularly in reference to claims of an adverse effect on competitiveness or job creation. *See* Marc Galanter, *Real World Torts: An Antidote to Anecdote,* 55 MD. L. REV. 1093, 1145–49 (1996).

of contract developed and as implied warranties made manufacturers strictly liable for losses from defective products, the tendency to analyze negligent or tortious liability with reference to physical harm was reinforced, lest the law of tort absorb that of contract.[152] But the difficulty endures, because damage to property is often nothing more (or less) than economic loss.

In a recent Supreme Court case, *Saratoga Fishing Co. v. J.M. Martinac & Co.*,[153] a manufacturer delivered a boat to the initial purchaser, who added equipment necessary for the vessel to engage in tuna fishing.[154] After the initial purchaser used the vessel and the added equipment and subsequently sold the vessel including the equipment to a second purchaser, the boat sank, allegedly because of a defect in the hydraulic system installed by the manufacturer.[155] Applying an admiralty tort doctrine that allows recovery for injuries caused by a defective product to "other property" but not to the defective product itself,[156] Justices Breyer and Scalia debated whether the added fishing equipment was part of the "product itself" for which the second purchaser could not recover damages in tort from the manufacturer or "other property" for which such damages could be recovered because the defective hydraulic system had caused damage to the added equipment.[157] Thus, it is the definition of "the property," the identity of the unit physically damaged, that becomes central.[158] Lost in the debate is

152. *See* FRIEDMAN, *supra* note 21, at 542 n.20; *see also* Schwartz, *supra* note 46, at 54–63.

153. 520 U.S. 875 (1997). The case was before the federal courts under admiralty jurisdiction; the tort law in admiralty is a judicial blend of federal and state tort law. *See id.* at 878.

154. *See id.*

155. *See id.*

156. *See* East River S.S. Corp. v. Transamerica Delaval Inc., 476 U.S. 858, 870 (1986) (adopting the economic loss doctrine for admiralty tort law and denying the purchaser of a defective product recovery for pure economic losses). The *East River* Court further stated: "[T]he resulting loss due to repair costs, decreased value, and lost profits is essentially the failure of the purchaser to receive the benefit of its bargain—traditionally the core concern of contract law." *Id.* at 870 (citation omitted).

157. *See Saratoga Fishing*, 520 U.S. at 884–85; *id.* at 888–89 (Scalia, J., dissenting). One complicating factor in *Saratoga Fishing* was the initial purchaser's use of the vessel following his adding the equipment: Was the product the vessel without the added equipment or was the equipment necessary before the vessel became the product? *See id.* at 878.

158. Justice Breyer and the majority found that the added equipment was "other property," making the manufacturer liable to a second purchaser for that equipment. *See id.* at 884–85. Justice Scalia insisted that the additional equipment was an integral part of the vessel, such that the purchaser, a commercial entity, could have recovered by warranty protection or not at all. *See id.* at 888–89 (Scalia, J., dissenting).

Justice Breyer and the majority defend their conclusion against the claim of "too great a potential [for] tort liability upon a manufacturer or distributor" by pointing out that "a host of other tort principles, such as forseeability, proximate cause, *and the 'economic loss' doctrine* already do, and would continue to, limit liability in important ways." *Id.* at 884 (emphasis

the common-sense observation that harm to the vessel and harm to the added equipment both involve property damage and economic loss. Splitting the vessel and its equipment into two classes of property, or uniting them as "the property," is simply not relevant to the question of whether a regime of negligence or of implied warranty more appropriately furthers corrective justice, promotes safety, or assigns risks sensibly. Thus, the classic division of contract and tort obscures the central issue of who bears the loss and why,[159] while at the same time suggesting that tortious conduct is only tangentially related to the injured party's economic well-being.[160]

The habit of focusing on physical integrity so as to minimize the inquiry about economic integrity appears in other areas of the legal system. Take work-related injuries and income, for example. Workers injured in connection with their employment suffer both economic and physical injury. To guarantee that such workers receive compensation and to shield employers from more expensive tort liability, the program of employer-funded workers' compensation sets a schedule of relatively automatic payments—so many dollars for a broken wrist, so much for a sprained back.[161] Whatever the merit of workers' compensation in delivering assured though limited payment for work-related injuries, one consequence of fixed schedules is a tendency to mute discussion of the economic impact on workers of job-related accidents: "Yes, she's not working, but she's got her comp." In this example, loss of income is conflated with recovery for a physical injury, and the cost to the wage earner of living on less than the expected weekly income becomes invisible. Equally problematic, the accidents themselves fade into

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added). Justice Scalia, in dissent, complains that tort protection should apply "only where contract-warranty protection is infeasible." *Id.* at 888 (Scalia, J., dissenting). His complaint arises in connection with his analysis of the physical injury issue under *Restatement (Second) of Torts* § 402A. *See id.* at 888–89 (Scalia, J., dissenting). Scalia's position seems to be that contract is primary—whether for reasons of economic efficiency, autonomy, or personal responsibility. *See* CANE, *supra* note 11, at 497–98. Logically, then, courts should analyze loss from the perspective of those unable to protect themselves through contract or insurance. *But see supra* text accompanying notes 141–43.

159. If the foundation of a building is faulty, causing a wall to collapse and also causing significant damage to cars parked alongside the building, the "other property" doctrine allows the car owners to sue in tort and the building owner to sue for damaged furniture, but it denies the building owner recourse for damages to the wall. *Cf. Saratoga Fishing*, 520 U.S. at 884–85.

160. Of course, some contractual relations are tainted by physical misconduct, like force and duress, and are therefore void. But this is an infinitesimal part of contract jurisprudence. For a good discussion, see HALE, *supra* note 20, at 109–33.

161. *See* John Fabian Witt, *The Transformation of Work and the Law of Workplace Accidents 1842-1910*, 107 YALE L.J. 1467, 1493–94 (1998).

the background, relegated to a routine risk of employment.[162] Thus, harms arising from quotidian transactions in the market are not perceived to create seriously injured parties or to generate severe consequences; nor is a job-related injury, which directly implicates economic security, seen as similar enough to injury occurring away from the workplace to require complete recovery.[163]

This brings us to the final part of the story, the rationale itself. Justice Cardozo's often repeated quote about the potential for indeterminate damages focused attention on the impact on the wrongdoer if recovery for pure economic loss were allowed, certainly a legitimate consideration. But tortious conduct injures "innocent" persons,[164] and the impact of a legal doctrine from their viewpoint also deserves attention. If we consider the ripple effects of pure economic loss from the perspective of the injured, the potential threat of substantial, disproportionate harm looks quite different. To take but one example, in *Stevenson*, the gas company's negligence cost the plaintiff more than a week's income, certainly significant from his point of view. Using the *Stevenson* court opinion as a springboard, one might argue:

> Cases might well occur where a manufacturer would be obliged to close down his factory [and the manufacturer's employees would be obliged to spend days idle and without income] because of the inability of [the manufacturer's] supplier due to a fire loss to make prompt deliveries; the [employees of a] power company with a contract to supply a factory with electricity would be deprived of [their income] which [they] would have made if the operations of the factory had not been interrupted by reason of fire damage; a

162. *Cf. id.* at 1497–98 (finding that workers recognized that state compensation programs deprived the community of public recognition of the employer's wrongful conduct). Unemployment compensation, offering a percentage of wages for a limited time in the expectation the involuntarily fired worker will find new employment, has a similar impact; and the troubling effects of massive job losses go largely ignored. *See* Susan C. Faludi, *The Reckoning*, WALL ST. J., May 16, 1990, at A1.

163. Consider the liability for causing a broken leg and loss of income from an automobile crash, as compared to the same broken leg caused by an accident on the job. Indeed, one could go further, as does Richard Abel, and question both the concept of compensatory damages as a legitimate part of relief for injury, *see* Richard L. Abel, *A Critique of American Tort Law*, 8 BRIT. J.L. & SOC'Y 199, 206–11 (1981), and the legitimacy of recovery for economic loss under any circumstances, *see* Richard L. Abel, *Should Tort Law Protect Property Against Accidental Loss?*, 23 SAN DIEGO L. REV. 79, 80 (1986). Abel criticizes, in my view correctly, the use of money as a substitute for freedom from pain or wholeness. *See id.* It is ironic, of course, that conditions not measurable in money are allowable damages while consequences like economic loss, measurable only in money, may be deemed immune from recovery.

164. Judge Kaufman recognized this in *Kinsman II*. *See supra* note 105.

> [person] who had a contract to paint [the worker's house] may not be able to proceed with [the] work; a [travel agent] who would have sold [the workers vacation packages] may be deprived of [her] commissions; the [teen-age gardener, the grocer's delivery person, the piano teacher, and the weekly housekeeper who service the worker's home and family] may [each] suffer a substantial loss. The claims of wor[kers] for loss of wages who were employed in such a factory and cannot continue to work there because of a fire, represent only a small fraction of the claims which would [go uncompensated] if recovery is [denied] in this class of cases. [Not to mention the mental distress of all affected when financial planning is compromised.][165]

Thus, economic injury from tortious conduct and its ripple effects may be severe and inescapable for the innocent victim and her peers, who rely on wages and the commerce they support. Yet the basis for choosing a liability principle that examines the impact on the wrongdoer and its business relations, rather than on the injured party and her peers, is rarely addressed.[166]

Reluctance to examine economic consequences from the perspective of the injured is not surprising. Market ideology tells us that if we work hard we will have economic security. It is frightening to contemplate, instead, that economic vulnerability is only one accident away. Even further, recovery for pure economic injury would call attention to the dangers of material insecurity in an economy that denies the ability of the market operating in the normal course of business to cause serious financial injury. Paradoxically, it may be easier to confront the speculative harm from emotional distress, because it does not implicate an organizing principle of our economy, than it is to acknowledge the proven damages from careless but familiar behavior.

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165. Stevenson v. East Ohio Gas Co., 73 N.E. 200, 203–04 (Ohio Ct. App. 1946); *see supra* notes 47–52 and accompanying text.

166. *But see* Louisiana *ex rel.* Guste v. M/V Testbank, 752 F.2d 1019, 1035–53 (5th Cir. 1985) (Wisdom, J., dissenting) ("Absent hard data, I would rather err on the side of receiving little additional benefit from imposing additional quanta liability than err by adhering to *Robins'* inequitable rule and bar victims' recovery on the mistaken belief that a 'marginal incentive curve' was flat, or nearly so. If a loss must be borne, it is no worse if a 'merely' negligent defendant bears the loss than an innocent plaintiff absorb the damages." (quotations in original)).

CONCLUSION

As noted earlier, this Essay is part of a project investigating the status of physical and economic integrity in various areas of the law. The cumulative findings from that larger project may or may not prove a systematic and unjustified privileging of physical over economic integrity. For now, it is enough to observe that the rule in tort denying claims of pure economic loss is partly right and importantly wrong. It is true that tortious conduct can cause economic injuries with consequences as dire as those arising from physical harms. Liability of indeterminate magnitude is, therefore, an appropriate concern in designing an injury compensation scheme. To conclude that all such claims must be denied is faulty, however, for as we have seen, the difference between damage to property and economic loss is frequently incoherent; causation and duty are capable of doing the job of containing liability by separating recoverable from unrecoverable losses; the wrongdoer may be in a better position to avoid the hazard and spread the risk, with insurance playing its customary role; and the fact that economic injury may be severe and inescapable does not tell us which party should bear that injury. Further, and here is the important wrongness, the categorical denial of the right to recover for pure economic injury does positive injustice to our understanding of the significance of material insecurity and economic integrity in American society.[167] Instead of clarifying the question of who bears the costs of potentially harmful but nonetheless desirable activity, the categorical no recovery rule obscures the logically antecedent question of which harms count. A rule which recognized pure economic loss from negligent conduct as compensable injury would illuminate this question by focusing attention on the significance of our economic well-being and its fragility.

Older readers may recall the Jack Benny routine in which the comedian hesitates when faced with the demand, "Your money or your life!" After an exaggerated pause, the holdup man demands, "Well?," to which Benny replies, "I'm thinking, I'm thinking!" The gag worked because, in taking the rhetorical question as offering a choice, Benny reinforced his well-established reputation as a cheapskate; only the tightest of fists could consider money more important than life. The consequences of denying recovery for

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167. Again, this Essay seeks to explain the anomalous treatment of pure economic loss in tort, not to argue that the treatment has created problems crying out for solution or that any particular reform is best.

economic loss are less dire than for resisting an armed robber, but oddly the presupposition is the same: Life, physical integrity, is always to be preferred over wealth, economic integrity. If this essay succeeds, it is because readers are prompted to speculate about other circumstances in which to merely ask a question such as "your money or your life?" is not to answer it.