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# Comments: Atlantis Revisited: Recovery under Maryland Law for Purely Economic Loss against Negligent Builders and Manufacturers

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# COMMENTS

## ATLANTIS REVISITED: RECOVERY UNDER MARYLAND LAW FOR PURELY ECONOMIC LOSS AGAINST NEGLIGENT BUILDERS AND MANUFACTURERS

### I. INTRODUCTION

Traditionally, building contractors and product manufacturers were not liable in tort for either personal injury or property damage to parties with whom they had no privity.<sup>1</sup> Building contractors owed duties only to those parties with whom they had a contract,<sup>2</sup> and not to the homeowner or third parties. Likewise, manufacturers owed duties only by virtue of their contract with the immediate purchaser of their product—either the distributor or the retailer—but not to the product's ultimate user.<sup>3</sup>

In the landmark decision of *MacPherson v. Buick Motor Co.*,<sup>4</sup> the New York Court of Appeals abolished the requirement of privity in negligence actions against manufacturers of defective products.<sup>5</sup> Judge Cardozo, writing for the court, held that a manufacturer may be liable in tort "irrespective of contract" for personal injuries

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1. For most of the 19th century, courts in both the United States and England denied negligence claims in the absence of privity of contract. In the seminal case of *Winterbottom v. Wright*, 152 Eng. Rep. 402 (1842), the English Court of Exchequer held that an injured passenger of a mail coach did not have a cause of action against the party under contract with the owner to keep the coach in repair. *Id.* at 404-06. According to the court, allowing a party not in privity to maintain an action would lead to "the most absurd and outrageous consequences, to which I can see no limit." *Id.* at 405. See also *Ford v. Sturgis*, 14 F.2d 253 (D.C. Cir. 1926) (denying recovery in tort to estate of theater patron killed by collapse of theater); *Huset v. J.I. Case Threshing Mach. Co.*, 120 F. 865 (8th Cir. 1903) (denying recovery in tort to an employee who suffered physical injury from defendant manufacturer's threshing machine).
  2. Typically, these parties are the developer or other subcontractors, including architects, surveyors and engineers. Annotation, *Negligence of Building or Construction Contractor as Ground of Liability upon His Part for Injury or Damage to Third Person Occurring After Completion and Acceptance of the Work*, 58 A.L.R.2d 865 (1958).
  3. See generally Michael D. Leider, *Constructing a New Action for Negligent Infliction of Economic Loss: Building on Cardozo and Coase*, 66 WASH. L. REV. 937, 943-44 (1991).
  4. 111 N.E. 1050 (N.Y. 1916).
  5. In *MacPherson*, the plaintiff was injured when a defective wheel on his automobile collapsed. *Id.* at 1051. He sued the manufacturer of the wheel despite the absence of privity. *Id.*

resulting from its negligence.<sup>6</sup> Cardozo noted that the court "put aside the notion that the duty to safeguard life and limb . . . grows out of contract and nothing else."<sup>7</sup>

The privity requirement has likewise been abolished in negligence actions against building contractors where personal injury is involved.<sup>8</sup> In *Inman v. Binghamton Housing Authority*,<sup>9</sup> a negligence action was brought against the architect of an apartment building for personal injuries suffered by a child who fell from a defective concrete porch.<sup>10</sup> The New York Court of Appeals denied the architect's privity defense and found that there was no meaningful distinction between injuries caused by chattels, as in *MacPherson*, and those involving building structures.<sup>11</sup>

The trend towards relaxation of the privity requirement has been slow to catch hold in cases where the resulting harm is characterized as an "economic loss." Generally, an economic loss is the loss of an expectancy interest created by contract, and occurs when a product or a building proves inferior in quality or does not perform for the purposes for which it is intended.<sup>12</sup> Economic losses may include such things as the loss of value or use of the product or building, the cost to repair or replace the product or building, or the lost profits resulting from the loss of use.<sup>13</sup>

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6. *Id.* at 1053, 1057.

7. *Id.* at 1053.

8. See generally 3 F. HARPER ET AL., *THE LAW OF TORTS* § 18.5, at 708-11 (2d ed. 1986) (delineating the erosion of privity in construction); James M. Dente, *Negligence Liability to all Foreseeable Parties for Pure Economic Harm: The Final Assault upon the Citadel*, 21 WAKE FOREST L. REV. 587, 587-89 (1986).

9. 143 N.E.2d 895 (N.Y. 1957).

10. *Id.* at 897.

11. *Id.* at 898-99.

12. See generally Sidney R. Barrett, Jr., *Recovery of Economic Loss in Tort for Construction Defects: A Critical Analysis*, 40 S.C. L. REV. 891, 894-97 (1989) (reviewing history of economic loss doctrine); Comment, *Manufacturers' Liability to Remote Purchasers for "Economic Loss" Damages—Tort or Contract?*, 114 U. PA. L. REV. 539, 541 (1966). The courts seldom adhere to a consistent definition of what types of damages are encompassed within the term "economic loss" and, in fact, are often simply confused by the entire issue. See Christopher C. Fallon, Jr., *Physical Injury and Economic Loss—The Fine Line of Distinction Made Clearer*, 27 VILL. L. REV. 483, 484-85 (1981-82). For example, in *Barnes v. Mac Brown & Co.*, 342 N.E.2d 619 (Ind. 1976), the court stated that all injuries, whether to person or property, ultimately result in economic loss. *Id.* at 621. See also *Cosmopolitan Homes, Inc. v. Weller*, 663 P.2d 1041, 1044 n.5 (Colo. 1983) (citing *Barnes* for the proposition that "both injury to one's person and injury to one's property result in economic loss").

13. *A.J. Decoster Co. v. Westinghouse Elec. Corp.*, 333 Md. 245, 250, 634 A.2d 1330, 1332 (1994); see also Barrett, *supra* note 12, at 892 n.1. For instance, if a farmer purchases a new tractor and finds that a part has to be replaced at

Because an economic loss is predicated upon the existence of a contract, courts have often been reluctant to allow a third person who is not a party to the contract to recover purely economic losses.<sup>14</sup> Historically, however, courts have not denied the recovery of economic losses to third parties in all circumstances. It is well-settled, for instance, that a third party may recover against building contractors or manufacturers for economic loss as a "parasitic" damage<sup>15</sup>—that is, when the economic loss is accompanied by physical harm to person or property.<sup>16</sup> The long-standing debate has been whether, absent privity of contract, a plaintiff may recover economic losses in a negligence action where there is no accompanying physical damage to person or property other than to the product or the structure itself.<sup>17</sup> The general rule adhered to by a majority of the states in both the manufacturing and construction contexts is often referred to as the "economic loss doctrine." Simply stated, with or without privity of contract, the economic loss doctrine holds that there is "no general duty to exercise reasonable care to avoid intangible economic loss or losses that do not arise from tangible physical harm to persons and tangible things."<sup>18</sup>

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a cost of \$500, this would be an economic loss. If the farmer also suffered \$1000 in lost profits to his business while the tractor was being repaired, this too would be an economic loss.

14. See W. PAGE KEETON ET AL., PROSSER AND KEETON ON THE LAW OF TORTS § 93, at 668-69 (5th ed. 1984).

15. Dente, *supra* note 8, at 589 n.20.

16. See KEETON ET AL., *supra* note 14, § 129, at 997. As the court stated in the oft-cited case, *People Express Airlines, Inc. v. Conrail Corp.*, 495 A.2d 107 (N.J. 1985):

The single characteristic that distinguishes parties in negligence suits whose claims for economic losses have been regularly denied by American and English courts from those who have recovered economic losses is, with respect to the successful claimants, the fortuitous occurrence of physical harm or property damage, however slight. It is well-accepted that a defendant who negligently injures a plaintiff or his property may be liable for all proximately caused harm, including economic losses.

*Id.* at 109.

Even in cases where the plaintiff has suffered physical harm and economic loss, the courts have recognized that the defendant is not liable for each and every consequence of his conduct, but only those that he proximately caused. *Palsgraf v. Long Island R.R.*, 162 N.E. 99, 100-01 (N.Y. 1928).

17. When economic loss has been sustained without any accompanying physical damage, other than to the product itself, most courts and commentators characterize the resultant harm as "pure economic harm." This Comment will use this definition of the term.

18. KEETON ET AL., *supra* note 14, § 92, at 657. This rule was consistently applied throughout the earlier part of this century. For instance, in the early case of *Robins Dry Dock & Repair Co. v. Flint*, 275 U.S. 303 (1927), the Supreme

There is little authority in Maryland regarding the rights of third parties to recover under the economic loss doctrine. The state's courts have adopted the rule of *MacPherson*,<sup>19</sup> and generally recognize that privity is not required for a third party to maintain a negligence action against a manufacturer for either personal injury or property damage.<sup>20</sup> The courts, however, have yet to identify fully in what instances purely economic losses are recoverable by third parties in tort actions against manufacturers and building contractors. A 1986 decision by the Court of Appeals of Maryland sheds light on the current status of the economic loss doctrine in Maryland. In *Council of Co-Owners Atlantis Condominium, Inc. v. Whiting-Turner Contracting Co.*,<sup>21</sup> the court held that

privity is not an absolute prerequisite to the existence of a tort duty . . . . [T]he duty of builders and architects . . . to use due care in the design, inspection, and construction of a building extends to those persons foreseeably subjected to the risk of personal injury because of a latent and unreasonably dangerous condition resulting from that negligence. . . . [W]here the dangerous condition is discovered before it results in injury, an action in negligence will lie for the recovery of the reasonable cost of correcting the condition.<sup>22</sup>

The *Atlantis* decision is a significant clarification of the status of both the privity defense and the economic loss doctrine in negli-

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Court denied recovery in negligence to time charterers who lost profits when the vessel they chartered was damaged while being repaired by the defendant dry dock company. *Id.* at 307. Justice Holmes found that the contract was between the dry dock company and the owners of the vessel; accordingly, the time charterers did not have a claim in contract or in tort for the lost profits. *Id.* at 309-10. *See also* *Byrd v. English*, 43 S.E. 419 (Ga. 1903) (denying recovery to owner of printing plant for lost profits incurred when defendant negligently damaged electrical conduits that supplied power to the plant); *Ultramares Corp. v. Touche, Niven & Co.*, 174 N.E. 441 (N.Y. 1931) (denying recovery to lender in negligence action against borrower's accountant for economic loss incurred as a result of reliance on a negligently prepared balance sheet); *Stevenson v. East Ohio Gas Co.*, 73 N.E.2d 200 (Ohio Ct. App. 1946) (denying recovery of lost wages to employee who was unable to work as a result of negligent rupture of stored natural gas tank at defendant's nearby utility plant).

19. 111 N.E. 1050 (N.Y. 1916).

20. *See, e.g.*, *Uppgren v. Executive Aviation Servs.*, 326 F. Supp. 709 (D. Md. 1971); *Babylon v. Scruton*, 215 Md. 299, 138 A.2d 375 (1958); *Kaplan v. Stein*, 198 Md. 414, 84 A.2d 81 (1951); *Excavation Constr., Inc. v. Mack Trucks, Inc.*, 576 F. Supp. 312 (D. Md. 1981).

21. 308 Md. 18, 517 A.2d 336 (1986).

22. *Id.* at 22, 517 A.2d at 338.

gence actions brought by third parties. The court of appeals not only rejected the privity defense and adopted, for the first time, a standard of foreseeability in determining the tort liability of building contractors to third parties, but it also suggested that purely economic loss may be recovered in such actions. The plaintiffs in *Atlantis* incurred neither property damage nor actual personal injury. By awarding them the reasonable cost of correcting dangerous building conditions where the mere risk of personal injury was present, the court effectively granted damages for purely economic loss. As the court reasoned, "the determination of whether a duty will be imposed in this type of case should depend upon the risk generated by the negligent conduct, rather than the fortuitous circumstance of the nature of the resultant damage."<sup>23</sup>

In Maryland's products liability area, two recent appellate decisions have applied the "risk of harm" approach set forth in *Atlantis*.<sup>24</sup> Although neither decision awarded the plaintiff economic losses, it is now evident that under Maryland law, a purchaser of a defective product may recover under a negligence theory for purely economic losses, including harm to the product itself, if the defect in the product causes a dangerous condition creating a risk of death or personal injury to the purchaser.<sup>25</sup>

This Comment first discusses some of the underpinnings of the economic loss doctrine, including policy reasons for its adoption. Second, this Comment explores the current viability of the economic loss doctrine in the United States and, in particular, under Maryland law in the areas of products liability and negligent construction.<sup>26</sup> Finally, this Comment will close with a discussion of *Atlantis* and other recent decisions, and their potential impact on the recovery of purely economic losses in Maryland.

## II. UNDERPINNINGS OF THE ECONOMIC LOSS DOCTRINE

One of the primary reasons advanced by the courts and various commentators in support of the economic loss doctrine is that re-

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23. *Id.* at 35, 517 A.2d at 345. Several other states have expressly denied recovery in tort for the mere risk of harm. *See, e.g.,* *Crowell Corp. v. Topkis Constr. Co.*, 280 A.2d 730 (Del. Super. Ct. 1971); *National Crane Corp. v. Ohio Steel Tube Corp.*, 332 N.W.2d 39 (Neb. 1983) (denying recovery in tort for expenses undertaken to repair defective parts of a crane which was in danger of collapsing); *Cincinnati Gas & Elec. Co. v. General Elec. Co.*, 656 F. Supp. 49 (S.D. Ohio 1986).
  24. *A.J. Decoster Co. v. Westinghouse Elec. Corp.*, 333 Md. 245, 634 A.2d 1330 (1994); *Morris v. Osmose Wood Preserving*, 99 Md. App. 646, 639 A.2d 147 (1994).
  25. *A.J. Decoster*, 333 Md. at 251-54, 634 A.2d at 1333-34; *Morris*, 99 Md. App. at 655-56, 639 A.2d at 152.
  26. This Comment superficially covers the recovery of pure economic losses under other causes of action such as strict liability, breach of warranty, and negligent misrepresentation. *See infra* part III.D.

covery of economic losses under tort law principles would expose contractors and manufacturers "to liability in an indeterminate amount for an indeterminate time to an indeterminate class."<sup>27</sup> As one commentator accurately noted, "only a limited amount of physical damage can ever ensue from a single act, while the number of economic interests a tortfeasor may destroy in a brief moment of carelessness is practically limitless."<sup>28</sup> For example, a driver who negligently causes a traffic accident during rush hour would certainly be responsible for the personal injuries suffered by those involved in the accident. It is doubtful, however, that the driver would also be held responsible for the provable losses suffered by truck drivers who were delayed as a result of the rush hour traffic jam or to the employee who was forced to clock in at work an hour late.<sup>29</sup> In order to place manageable limits on liability in negligence actions, the requirement of some type of physical harm, measurable and identifiable, has been established as a necessary element of the causal relationship between a plaintiff's economic harm and the defendant's negligence.<sup>30</sup> Most courts, therefore, have recognized that economic loss is recoverable only when it is accompanied by physical damage, such as parasitic damage.<sup>31</sup> When only economic harm is incurred, the courts have traditionally denied recovery in tort.<sup>32</sup>

Another reason advanced in support of the economic loss doctrine is that economic losses are the type of damages which have traditionally been covered by principles of contract and warranty

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27. *Ultramares Corp. v. Touche, Niven & Co.*, 174 N.E. 441, 444 (N.Y. 1931). Justice Cardozo continued, "[t]he 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 duty that exposes to these consequences." *Id.*
  28. Comment, *Foreseeability of Third Party Economic Injuries—A Problem in Analysis*, 20 U. CHI. L. REV. 283, 298 (1953).
  29. *In re Kinsman Transit Co.*, 388 F.2d 821, 825 n.8 (2d Cir. 1968).
  30. Kelly M. Hnatt, Comment, *Purely Economic Loss: A Standard for Recovery*, 73 IOWA L. REV. 1181, 1190-94 (1988).
  31. Indeed, when a defendant's conduct results in some type of physical harm, either to the plaintiff's person or property other than the product itself, the resulting loss is not "economic." See *supra* part III.A-B. There is considerable debate regarding whether damage to the product itself constitutes economic loss, which is generally not recoverable in negligence, and under what circumstances damage to property "other than the product itself" may constitute recoverable property damage. See *supra* part III.A-B.
  32. See, e.g., *Byrd v. English*, 43 S.E. 419, 420-21 (Ga. 1903) (denying recovery by commercial printer against contractor whose negligence caused downed power lines and resulted in loss of power to the plaintiff's presses); *Brink v. Wabash R.R.*, 60 S.W. 1058, 1059-60 (Mo. 1901) (denying recovery against defendant who negligently derailed train which resulted in death of plaintiff's son, thereby preventing son from carrying out his contractual obligations to support plaintiff).

law, not tort law. Economic harm is typically incurred when a product or building fails to meet the expectations of the buyer, or when the only loss sustained is the cost of repair or replacement, the consequent loss of profits, or the diminution in value.<sup>33</sup> When the defect in a product or building structure is of such a qualitative nature, principles of contract and warranty law provide the appropriate remedy.<sup>34</sup> Contract law protects expectancy interests and provides the appropriate set of rules when a purchaser wants a product to perform in a certain way, or expects the product to be of a particular quality or fit for a particular use.<sup>35</sup> In addition, contracts perform the important function of allocating risks among the parties, including the risk that profits will be lost if the product fails. Tort law, in contrast, imposes standards of reasonable care upon all persons to avoid causing foreseeable harm to the person or property of others.<sup>36</sup> Recovery of economic loss under tort principles, it is argued, would frustrate the risk-allocating function of contracts.

Several leading cases have also applied the economic loss doctrine to deny recovery in tort for purely economic loss on the basis that the Uniform Commercial Code (UCC) adequately provides for the recovery of such losses through express or implied warranties.<sup>37</sup> The Supreme Court of Idaho, for instance, found no compelling reason to extend negligence principles "into an area in which the legislature [had] already enacted comprehensive legislation, thereby undermining that legislation."<sup>38</sup> The court reasoned that "the UCC provisions

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33. See generally Barrett, *supra* note 12, at 894-95.

34. See generally Comment, *Manufacturer's Liability to Remote Purchasers for "Economic Loss" Damages—Tort or Contract?*, 114 U. PA. L. REV. 539 (1966); see also *Pennsylvania Glass Sand Corp. v. Caterpillar Tractor Co.*, 652 F.2d 1165, 1172-73 (3d Cir. 1981) (holding that buyer was not precluded from seeking tort recovery because damage to front-end loader constituted physical rather than economic injury); *Moorman Mfg. Co. v. National Tank Co.*, 435 N.E.2d 443, 451 (Ill. 1982) (holding that crack in grain storage tank constituted economic loss for which buyer could recover in contract only).

35. Barrett, *supra* note 12, at 901-02.

36. *Id.*

37. See, e.g., *2000 Watermark Ass'n v. Celotex Corp.*, 784 F.2d 1183, 1186 (4th Cir. 1986); *Jones & Laughlin Steel Corp. v. Johns-Manville Sales Corp.*, 626 F.2d 280, 288-91 (3d Cir. 1980); *Seely v. White Motor Co.*, 403 P.2d 145, 151-52 (Cal. 1965); *Clark v. International Harvester Co.*, 581 P.2d 784, 792-94 (Idaho 1978); *Moorman Mfg. Co. v. National Tank Co.*, 435 N.E.2d 443, 447-48 (Ill. 1982) ("[I]t is preferable to relegate the consumer to the comprehensive scheme of remedies fashioned by the UCC, rather than requiring the consuming public to pay more for their products so that a manufacturer can insure against the possibility that some of his products will not meet the business needs of some of his customers."); *Nelson v. Todd's Ltd.*, 426 N.W.2d 120, 125 (Iowa 1988).

38. *Clark v. International Harvester Co.*, 581 P.2d 784, 794 (Idaho 1978).



adequately define the rights of the parties in such cases and that judicial expansion of negligence law to cover purely economic losses would only add more confusion in an area already plagued with overlapping and conflicting theories of recovery."<sup>39</sup>

Other courts argue that permitting recovery of economic losses in tort would make it virtually impossible for a manufacturer to sell a product "as is."<sup>40</sup> The UCC is based upon the principle that parties should be free to make contracts as they choose, including contracts that disclaim liability for breaches of warranty.<sup>41</sup> Conversely, those courts that do not adhere to the economic loss rule have no difficulty reconciling the recovery of economic loss in negligence actions with the no-fault liability scheme of the UCC.<sup>42</sup> These courts reason that a manufacturer should owe a duty of care to users of its products to prevent foreseeable harm, and that economic loss from defective products is "within the range of reasonable manufacturer foresight."<sup>43</sup>

### III. RECOVERY OF PURELY ECONOMIC LOSS IN NEGLIGENCE ACTIONS AGAINST MANUFACTURERS

In the area of manufacturing defects, an overwhelming majority of courts in the country have held that a purchaser of a defective

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39. *Id.*

40. *See, e.g.,* 2000 Watermark Ass'n, Inc. v. Celotex Corp., 784 F.2d 1183 (4th Cir. 1986), in which the Fourth Circuit stated:

The UCC is generally regarded as the exclusive source for ascertaining when the seller is subject to liability for damages if the claim is based on an intangible economic loss and not attributable to physical injury to person or to a tangible thing other than the defective product itself.[citation omitted] If intangible economic loss were actionable under a tort theory, the UCC provisions permitting assignment of risk by means of warranties and disclaimers would be rendered meaningless. It would be virtually impossible for a seller to sell a product "as is" because if the product did not meet the economic expectations of the buyer, the buyer would have an action under tort law. The UCC represents a comprehensive statutory scheme which satisfies the needs of the world of commerce, and courts have been reluctant to extend judicial doctrines that might dislocate the legislative structure.

*Id.* at 1186 (citation omitted).

41. Spring Motors Distribs., Inc. v. Ford Motor Co., 489 A.2d 660, 668 (N.J. 1985). "[T]he UCC is the more appropriate vehicle for resolving commercial disputes arising out of business transactions between persons in a distributive chain." *Id.*

42. *See, e.g.,* Western Seed Prod. Corp. v. Campbell, 442 P.2d 215 (Or. 1968); Berg v. General Motors Corp., 555 P.2d 818 (Wash. 1976).

43. *Western Seed*, 442 P.2d at 218 (quoting Marc A. Franklin, *When Worlds Collide: Liability Theories and Disclaimers in Defective-Product Cases*, 18 STAN. L. REV. 974, 989 (1966)).

product may not recover purely economic losses in a negligence action against a manufacturer.<sup>44</sup> These courts generally permit recovery only for actual physical harm, either in the form of personal injury to the plaintiff or in the form of damage to "other property," that is, injury to property other than the product itself.<sup>45</sup> When injury is sustained by only the product itself, it is typically in the form of deterioration, internal breakdown, or some other failure of the product to meet the purchaser's expectations.<sup>46</sup> This type of damage is characterized as economic in nature<sup>47</sup> and, it is argued, is more properly governed by contract or warranty law, rather than tort law principles.<sup>48</sup>

#### *A. The Requirement of Physical Damage to Property Other Than the Product Itself*

The requirement that physical damage be incurred to property other than the product itself has been adopted by most courts and has proven to be a significant barrier to recovery in tort.<sup>49</sup> In one

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44. For some of the leading cases denying recovery of purely economic losses in negligence actions, see 2000 Watermark Ass'n v. Celotex Corp., 784 F.2d 1183 (4th Cir. 1986); Sanco, Inc. v. Ford Motor Co., 771 F.2d 1081, 1086 (7th Cir. 1985); Jones & Laughlin Steel Corp. v. Johns-Manville Sales Corp., 626 F.2d 280 (3d Cir. 1980); Arizona v. Cook Paint & Varnish Co., 391 F. Supp. 962 (D. Ariz. 1975); Long v. Jim Letts Oldsmobile, Inc., 217 S.E.2d 602 (Ga. Ct. App. 1975); Clark v. International Harvester Co., 581 P.2d 784 (Idaho 1978); Moorman Mfg. Co. v. National Tank Co., 435 N.E.2d 443 (Ill. 1982); Alfred N. Koplín & Co., Inc. v. Chrysler Corp., 364 N.E.2d 100 (Ill. App. Ct. 1977) (denying recovery in negligence action against manufacturer for cost of repairing and replacing defective air conditioners); Clevenger & Wright Co. v. A.O. Smith Harvester Prods., Inc., 625 S.W.2d 906 (Mo. Ct. App. 1981); National Crane Corp. v. Ohio Steel Tube Co., 332 N.W.2d 39 (Neb. 1983).

45. See generally Barrett, *supra* note 12, at 894-97.

46. See generally Note, *Economic Loss in Products Liability Jurisprudence*, 66 COLUM. L. REV. 917, 918 (1966).

47. The Supreme Court of South Carolina, in Kennedy v. Columbia Lumber & Manufacturing Co., 384 S.E.2d 730 (S.C. 1989), stated that "[t]he 'economic loss rule' simply states that there is no tort liability for a product defect if the damage suffered by the plaintiff is only to the product itself. In other words, tort liability only lies where the damage done is to other property or is personal injury." *Id.* at 734.

48. See, e.g., 2000 Watermark Ass'n v. Celotex Corp., 784 F.2d 1183 (4th Cir. 1986); R.W. Murray Co. v. Shatterproof Glass Corp., 697 F.2d 818 (8th Cir. 1983); Pennsylvania Glass Sand Corp. v. Caterpillar Tractor Co., 652 F.2d 1165, 1169-72 (3d Cir. 1981).

49. See, e.g., R.W. Murray Co. v. Shatterproof Glass Corp., 697 F.2d 818 (8th Cir. 1983) (holding that diminution in value of building and lost rent incurred as a result of negligent manufacture of glass panels were merely economic losses and not recoverable in tort); City of Greenville v. W.R. Grace & Co., 640 F. Supp. 559, 564 (D. S.C. 1986) (holding that manufacturer could be

of the most oft-cited cases, *Moorman Manufacturing Co. v. National Tank Co.*,<sup>50</sup> a plaintiff purchased a grain storage tank from the defendant who designed and manufactured the tanks.<sup>51</sup> When a crack developed in the tank because of a defect, the plaintiff brought suit in negligence and strict liability for the cost of repairs, and for loss of use of the tank.<sup>52</sup> The Supreme Court of Illinois denied recovery against the manufacturer under both negligence and strict liability theories.<sup>53</sup> The court reasoned that the crack in the tank was not the type of "sudden and dangerous occurrence" that tort law was designed to protect.<sup>54</sup> Instead, the law of warranty afforded the plaintiff the proper measure of protection against commercial losses of this nature.<sup>55</sup> The repair of the tank and the loss of its use were economic losses, and the plaintiff's only remedy lied in contract.<sup>56</sup>

The distinction between damage that has occurred to "other property" and damage to the product itself is a difficult line to draw, and those courts attempting to do so are seldom consistent. In *2000 Watermark Ass'n. v. Celotex Corp.*,<sup>57</sup> a homeowner's association sued the manufacturer of asphalt shingles in negligence when blisters appeared on the shingles, shortening their expected life.<sup>58</sup> The association argued that the removal of the defective shingles caused actual property damage, not mere economic loss, because the under-

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liable in negligence for contamination of building caused by asbestos), *aff'd*, 827 F.2d 975 (4th Cir. 1987); *Agristor Leasing v. Guggisberg*, 617 F. Supp. 902, 908 (D. Minn. 1985) (denying recovery against manufacturer of animal feed storage system for damage to feed on basis that feed was not "other property"); *Arrow Leasing Corp. v. Cummins Ariz. Diesel, Inc.*, 666 P.2d 544, 547-49 (Ariz. Ct. App. 1983) (holding that plaintiff could not recover in negligence and strict liability against manufacturer of turbo-charger component of tractor for damage caused only to turbo-charger itself and engine; also holding for first time that when component part of product damages another component part, resulting harm may constitute damage to "other property," but not when damaged part was also provided by same vendor); *Chrysler Corp. v. Taylor*, 234 S.E.2d 123 (Ga. Ct. App. 1977); *Clark v. International Harvester Co.*, 581 P.2d 784 (Idaho 1978); *Moorman Mfg. Co. v. National Tank Co.*, 435 N.E.2d 443 (Ill. 1982); *St. Paul Fire & Marine Ins. Co., v. Steeple Jac Inc.*, 352 N.W.2d 107, 109 (Minn. Ct. App. 1984) (holding that defective gear box, which caused window washing unit to fall from plaintiff's building, was not actionable in negligence since there was no damage to persons or other property); *Inglis v. American Motors Corp.*, 209 N.E.2d 583 (Ohio 1965).

50. 435 N.E.2d 443 (Ill. 1982).

51. *Id.* at 445.

52. *Id.*

53. *Id.* at 451-52.

54. *Id.* at 450.

55. *Id.*

56. *Id.*

57. 784 F.2d 1183 (4th Cir. 1986).

58. *Id.* at 1185.

lying tar paper had also been damaged and needed to be replaced before new shingles could be installed.<sup>59</sup> Applying South Carolina law, the Fourth Circuit found that no property damage aside from the defective shingles had been incurred.<sup>60</sup> According to the court, the expenses associated with replacement of the tar paper were only incidental in nature and would be recoverable only in a warranty action, not an action for negligence.<sup>61</sup>

In contrast, in *Minneapolis Society of Fine Arts v. Parker-Klein*,<sup>62</sup> the Supreme Court of Minnesota indicated that this type of incidental damage might give rise to recovery in negligence on the basis that damage was incurred by "other property."<sup>63</sup> The plaintiff in *Parker-Klein* brought suit in negligence and strict liability against the manufacturer of brick used in the construction of the exterior walls of two buildings.<sup>64</sup> Shortly after construction, the brick proved defective and began to crack, craze, and spall.<sup>65</sup> The court found that the record did not support the plaintiff's claim that property apart from the brick itself was physically damaged, particularly since the brick was used for non-load-bearing walls and because the repairs to the buildings were completed without affecting their underlying structure.<sup>66</sup> The court noted, however, that the failure of the brick had caused damage to the mortar between the bricks, and acknowledged that this might constitute damage to "other property."<sup>67</sup> However, the plaintiff had not provided a breakdown of the cost to repair the mortar, and the court refused to allow the plaintiff to sue in tort for six million dollars solely by virtue of the relatively minor damages to the mortar.<sup>68</sup>

The United States Supreme Court has addressed the "other property" requirement on only one occasion. In *East River Steamship Corp. v. Transamerica Delaval, Inc.*,<sup>69</sup> the plaintiff was a shipbuilder who had contracted with a turbine manufacturer to design, manufacture, and install turbines in four vessels.<sup>70</sup> When the ships were put into service, the turbines in all four vessels malfunc-

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59. *Id.* at 1187.

60. *Id.* at 1187-88.

61. *Id.*

62. 354 N.W.2d 816 (Minn. 1984), *overruled by* Hapka v. Paquin Farms, 458 N.W.2d 683 (Minn. 1990).

63. *Id.* at 820-21.

64. *Id.* at 817.

65. *Id.* at 818.

66. *Id.* at 820.

67. *Id.* at 820 n.4.

68. *Id.*

69. 476 U.S. 858 (1986).

70. *Id.* at 859.

tioned.<sup>71</sup> The shipbuilder sued the manufacturer for the cost of repairing the turbines and for lost profits, alleging that the manufacturer was strictly liable for design defects and that it negligently supervised the installation of one of the turbines.<sup>72</sup>

The Court reviewed the majority and minority approaches to the issue of economic loss. The majority approach, according to the Court, holds that damage to a product itself is a purely monetary loss that is more properly covered by warranty law.<sup>73</sup> The minority view holds that a manufacturer's duty to produce a product that is not defective encompasses injury to the product itself.<sup>74</sup> Finding the minority view unpersuasive, the Court unanimously held that a manufacturer owes no duty under either a negligence or strict liability theory to prevent a product from damaging itself.<sup>75</sup> In this circumstance, when no person or other property is damaged, the resulting loss is purely economic and is best addressed by contractual remedies.<sup>76</sup>

Only a few courts have found that economic loss, in the absence of any damage to either persons or other property, is recoverable in negligence actions.<sup>77</sup> These courts permit recovery regardless of whether the damage is only to the product itself, and irrespective of the manner in which the harm occurred.<sup>78</sup> Instead, these courts focus on the foreseeability of the resulting harm as the principal determinant of liability.

In *Berg v. General Motors Corp.*,<sup>79</sup> the plaintiff was a commercial fisherman who sued for lost profits incurred when the diesel boat engine manufactured by the defendant broke down due to an error in factory assembly.<sup>80</sup> The Supreme Court of Washington rejected the defendant's privity defense and its argument that the pecuniary losses suffered by the plaintiff were not recoverable in the absence of any property damage.<sup>81</sup> The court found that the negligent

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71. *Id.* at 860-61.

72. *Id.* at 861.

73. *Id.* at 868 (citing *Seely v. White Motor Co.*, 403 P.2d 145 (Cal. Ct. App. 1965)).

74. *Id.* at 868-69 (citing *Santor v. A & M Karagheusian, Inc.*, 207 A.2d 305 (N.J. 1965)).

75. *Id.* at 871.

76. *Id.* at 870-71.

77. *Western Seed Prod. Corp. v. Campbell*, 442 P.2d 215 (Or. 1968); *Nobility Homes v. Shivers*, 557 S.W.2d 77 (Tex. 1977) (affirming judgment for plaintiff in negligence without discussion); *Berg v. General Motors Corp.*, 555 P.2d 818 (Wash. 1976).

78. *See supra* part III.A.

79. 555 P.2d 818 (Wash. 1976), *superseded by* WASH. REV. CODE § 7.72 *et seq.* (1993).

80. *Id.* at 818-19.

81. *Id.* at 822-23.

manufacture of the engine created the foreseeable risk that the plaintiff's enterprise would be halted and that lost profits would be incurred.<sup>82</sup> The court failed to recognize any "distinction that would allow recovery if the product in question destroyed the property of another, yet would deny recovery were the same product merely to disintegrate."<sup>83</sup> The requirement of personal injury or property damage, the court reasoned, only inheres in strict liability actions.<sup>84</sup> The court therefore concluded that "nothing in the tort of negligence . . . prevents lost profits from being a specie of recompensable harm which is actionable against the remote manufacturer."<sup>85</sup>

The Supreme Court of Oregon has also allowed recovery for purely economic loss. In *State ex rel. Western Seed Production Corp. v. J.R. Campbell*,<sup>86</sup> the court held that sugar beet farmers could recover in negligence for crop losses caused by defects in seeds manufactured by the defendant.<sup>87</sup> The court acknowledged that other courts limited negligence liability for purely economic losses to situations in which the loss occurred "in a violent or dangerous accident."<sup>88</sup> The court, however, saw no reason why the availability of a tort remedy should depend on whether the damage occurs in a traumatic fashion.<sup>89</sup> A manufacturer, it stated, should owe a duty to avoid foreseeable harm to the users of its product.<sup>90</sup>

#### B. The "Sudden and Calamitous" Exception

In recent years, an intermediate form of the economic loss doctrine—or perhaps more accurately, an exception to it—has developed. This exception permits recovery in negligence or strict liability for injury to the product itself when the damage occurs in a sudden, calamitous, and dangerous manner.<sup>91</sup> Rather than focus on

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82. *Id.* at 823.

83. *Id.* at 822.

84. *Id.* at 823.

85. *Id.* Although the court failed to make such a distinction, this decision was decided under admiralty law, as were the decisions relied upon by the court.  
*Id.*

86. 442 P.2d 215 (Or. 1968), *cert. denied*, 393 U.S. 1093 (1969).

87. *Id.* at 218-19.

88. *Id.* at 218.

89. *Id.*

90. *Id.*

91. *See, e.g., Agristor Leasing v. Guggisberg*, 617 F. Supp. 902, 908 n.4 (D. Minn. 1985) (holding that damage to animal feed caused by defendant's feed storage system "was not caused by sudden calamitous occurrence, but was a rise of product ineffectiveness"); *Sanco, Inc. v. Ford Motor Co.*, 579 F. Supp. 893 (S.D. Ind. 1984), *aff'd*, 771 F.2d 1081 (7th Cir. 1985) (stating that economic loss may not be recovered in negligence action based on a sudden and calamitous occurrence); *Cloud v. Kit Mfg. Co.*, 563 P.2d 248, 251 (Alaska 1977) (holding

whether damage has occurred to "other property," the exception focuses instead on the nature of the defect and the manner in which the damage occurred.<sup>92</sup> When the defect in the product results in deterioration, internal breakage, depreciation, or failure to live up to the purchaser's expectations, courts invoking this exception will permit recovery only under contract or warranty law.<sup>93</sup> However, where the damage results in a hazardous condition, through a sudden and calamitous occurrence, these same courts permit recovery under tort law.<sup>94</sup> The "sudden and calamitous" exception, as one court observed, marks the distinction between "the disappointed users . . . and the endangered ones."<sup>95</sup>

In *Pennsylvania Glass Sand Corp. v. Caterpillar Tractor Co.*,<sup>96</sup> one of the leading cases on this subject, the Third Circuit addressed whether, under Pennsylvania law, an accidental injury to a product itself as a result of a hazardous defect would constitute economic loss or physical property damage.<sup>97</sup> The plaintiff, in *Caterpillar*, had purchased a front-end tractor loader from the defendant manufacturer and used it without incident for four years.<sup>98</sup> While the loader was in operation, a fire suddenly broke out and the machine was severely damaged.<sup>99</sup> The court stated:

In cases such as the present one where only the defective product is damaged, the majority approach is to identify whether a particular injury amounts to economic loss or physical damage. In drawing this distinction, the items for

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that damage to trailer from fire caused by the ignition of polyurethane padding in carpet of trailer was "sudden and calamitous" damage and not deterioration, internal breakage, or depreciation that would be considered economic loss); *Moorman Mfg. Co. v. National Tank Co.*, 435 N.E.2d 443, 450 (Ill. 1982) (holding that crack that developed in grain storage tank was not sudden and dangerous occurrence, but rather "a qualitative defect relating to the purchaser's expectation in terms of the product's fitness to perform its intended function"); *Industrial Uniform Rental Co. v. International Harvester Co.*, 463 A.2d 1085 (Pa. Super. Ct. 1983); see also Barrett, *supra* note 12, at 914-16; Note, *Economic Loss in Products Liability Jurisprudence*, 66 COLUM. L. REV. 917, 918 (1966).

92. See *Pennsylvania Glass Sand Corp. v. Caterpillar Tractor Co.*, 652 F.2d 1165 (3d Cir. 1981); *Sanco, Inc. v. Ford Motor Co.*, 579 F. Supp. 893 (S.D. Ind. 1984), *aff'd*, 771 F.2d 1081 (7th Cir. 1985).

93. *Minneapolis Soc'y of Fine Arts v. Parker-Klein Assocs. Architects, Inc.*, 354 N.W.2d 816, 821 (Minn. 1984), *overruled in part by Hapka v. Panquin Farms*, 458 N.W.2d 683 (Minn. 1990).

94. *Id.* at 821.

95. *Russell v. Ford Motor Co.*, 575 P.2d 1383, 1387 (Or. 1978).

96. 652 F.2d 1165 (3d Cir. 1981).

97. *Id.* at 1166-67.

98. *Id.* at 1166.

99. *Id.*

which damages are sought, such as repair costs, are not determinative. Rather, the line between tort and contract must be drawn by analyzing interrelated factors such as *the nature of the defect, the type of risk, and the manner in which the injury arose*.<sup>100</sup>

Applying these factors, the Third Circuit found that the nature of the risk, a fire, was a "sudden and highly dangerous occurrence,"<sup>101</sup> and that the alleged defect, a faulty design in the hydraulic line, constituted "a safety hazard that posed a serious risk of harm to person and property."<sup>102</sup> The court therefore held that under Pennsylvania law, damages incurred to the product itself would not be treated as an economic loss when the injury stemmed from a hazardous defect and was brought about by a sudden and highly dangerous occurrence.<sup>103</sup>

Several courts appear to have adopted a variation of the sudden and calamitous exception that permits recovery in tort for damage to the product itself, but only where the damage takes place in a manner that creates an identifiable risk of injury to persons or other property.<sup>104</sup> Stated otherwise, sudden, violent damage to the product itself would be insufficient to permit recovery in tort if the product posed no threat to anything or anyone other than the product itself. For example, in *Northern Power & Engineering Corp. v. Caterpillar Tractor Co.*,<sup>105</sup> the plaintiff sued the manufacturer of an electric generator when the oil pressure valve of the generator failed to function, causing severe damage to the engine.<sup>106</sup> Although the damage occurred in a sudden manner, no persons or other property were harmed.<sup>107</sup> The court therefore denied the plaintiff's tort claim.<sup>108</sup>

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100. *Id.* (emphasis added). As another court has noted:

Deciding whether there was a violent occurrence does not depend on the nature of the product. It depends on the nature of the incident that caused the damage. . . . [E]xploding bottles, runaway barges, flying saw blades, and incendiary packages [are the] types of accidents that are likely to cause bodily injuries or damage to other products that are traditionally recoverable in tort.

*City of Clayton v. Grumman Energy Prods., Inc.*, 576 F. Supp. 1122, 1126 (E.D. Mo. 1983).

101. *Pennsylvania Glass Sand Corp. v. Caterpillar Tractor Co.*, 652 F.2d 1165, 1174 (3d Cir. 1981).

102. *Id.*

103. *Id.* at 1175.

104. *See, e.g.*, *Northern Power & Eng'g Corp. v. Caterpillar Tractor Co.*, 623 P.2d 324 (Alaska 1981); *Cloud v. Kit Mfg. Co.*, 563 P.2d 248 (Alaska 1977); *Russell v. Ford Motor Co.*, 575 P.2d 1383 (Or. 1978).

105. 623 P.2d 324 (Alaska 1981).

106. *Id.* at 326.

107. *Id.* at 329.

108. *Id.* at 330.



The United States Supreme Court has altogether rejected the "sudden and calamitous" exception in *East River Steamship Corp. v. Transamerica Delaval, Inc.*<sup>109</sup> The petitioner in *East River* filed an admiralty complaint against Transamerica, alleging that it was strictly liable for certain design defects in turbines installed in the petitioner's vessels.<sup>110</sup> In examining whether the remedy for damages to the turbines properly lied in a tort action, the Court observed that even where the harm to the product occurs through an abrupt, accident-like event, "the 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."<sup>111</sup> The "maintenance of product value and quality is precisely the purpose of express and implied warranties."<sup>112</sup> The concern for personal safety evidence by tort law is reduced or not implicated when the injury is only to the product itself.<sup>113</sup>

### C. A Manufacturer's Liability Under Maryland Law for Economic Loss

Maryland's appellate courts have recently adopted a novel approach to the recovery of economic loss in the context of a products liability action. Applying the "risk of harm" analysis first set forth in the *Atlantis* decision, the court of appeals in *A.J. Decoster v. Westinghouse Electric Corp.*<sup>114</sup> and the court of special appeals in

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109. 476 U.S. 858 (1986).

110. *Id.* at 861.

111. *Id.* at 870. Deans Prosser and Keeton have observed:

Making liability depend upon whether or not the loss results from an "accident" creates a difficult issue and arguably an irrelevant issue with respect to the validity of contract provisions allocating the risk of loss for harm to the defective product itself to the purchaser. Distinguishing "accidental" damage to the product from mere economic loss is difficult in many cases.

KEETON ET AL., *supra* note 14, § 101(3), at 709.

112. *East River*, 476 U.S. at 872.

113. *Id.* at 871-72. Dean Keeton appears to agree with the Supreme Court. He has stated:

A distinction should be made between the type of "dangerous condition" that causes damage only to the product itself and the type that is dangerous to other property or persons. A hazardous product that has harmed something or someone can be labeled a part of the accident problem; tort law seeks to protect against this type of harm through allocation of risk. In contrast, a damaging event that harms only the product should be treated as irrelevant to policy considerations directing liability placement in tort. Consequently, if a defect causes damage limited solely to the property, recovery should be available if at all on a contract-warranty theory.

W. Page Keeton, *Annual Survey of Texas Law on Torts*, 32 Sw. L.J. 1 (1978).

114. 333 Md. 245, 634 A.2d 1330 (1994).

*Morris v. Osmose Wood Preserving*<sup>115</sup> have held that a plaintiff may recover under a negligence theory for purely economic losses, including harm to the product itself, if the defect in the product causes a dangerous condition creating a risk of death or personal injury to the consumer.<sup>116</sup> Although the courts in *A.J. Decoster* and *Morris* did not ultimately award economic losses to the plaintiffs, the decisions mark an important turning point in Maryland law in the products liability area.

In *A.J. Decoster*, the court of appeals addressed for the first time in the products liability setting, the "distinction between property loss and pure economic loss in determining whether a claim may be brought under a tort or contract theory or both."<sup>117</sup> The plaintiff in the suit was a commercial chicken and egg producer who purchased an electrical transfer switch designed to detect and respond to any loss of electrical power in the ventilation system at its chicken houses.<sup>118</sup> When a power failure occurred, the switch did not sense the loss of power and failed to activate the backup power system.<sup>119</sup> As a result, the plaintiff's ventilation system overheated and shut down, suffocating over 140,000 chickens.<sup>120</sup> The plaintiff filed suit against Westinghouse, the manufacturer of the switch, alleging counts of negligence, strict liability, and breach of warranty.<sup>121</sup> Westinghouse sought to dismiss the negligence claim on the basis that the plaintiff had alleged only economic losses.<sup>122</sup>

The court of appeals framed the issue in *A.J. Decoster* as whether the plaintiff's damages could be considered "physical harm or economic losses and, if the latter, whether the defective switch caused a dangerous condition creating a risk of death or personal injury to humans."<sup>123</sup> The court did not reach the second part of this determination because it found that the death of the plaintiff's chickens was a loss of physical property, rather than an economic loss, and was therefore recoverable.<sup>124</sup> The court reasoned that the plaintiff was not seeking to recover the loss of the value of the

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115. 99 Md. App. 646, 639 A.2d 147, *cert. granted*, 336 Md. 98, 646 A.2d 1018 (1994).

116. *A.J. Decoster*, 333 Md. at 251-53, 634 A.2d at 1333-34; *Morris*, 99 Md. App. at 654-55, 639 A.2d at 151-52.

117. 333 Md. at 247, 634 A.2d at 1331.

118. *Id.* The plaintiff originally alleged that it purchased the switch from Westinghouse, the manufacturer, but later conceded that it purchased the switch from a dealer. *Id.* at 248 n.1, 634 A.2d at 1331 n.1.

119. *Id.* at 247, 634 A.2d at 1331.

120. *Id.* at 247-48, 634 A.2d at 1331.

121. *Id.*

122. *Id.* at 248-49, 634 A.2d at 1331-32.

123. *Id.* at 251, 634 A.2d at 1333.

124. *Id.*

switch, the costs to repair or replace the switch, or any lost profits from the plaintiff's diminished egg production.<sup>125</sup> Rather, the plaintiff sought the replacement value of the chickens, which constituted property that was "wholly distinct from the allegedly defective product."<sup>126</sup> The court held that a manufacturer may be held liable for physical harm to person or property, other than the product itself, caused by defects in its products "because it is charged with the responsibility to ensure that its products meet a standard of safety creating no unreasonable risk of harm."<sup>127</sup>

The court of special appeals was faced with a more challenging situation in *Morris v. Osmose Wood Preserving*,<sup>128</sup> where there was no damage to "other property." The plaintiffs in *Morris* were a group of homeowners who alleged that the fire retardant treated (FRT) plywood used to construct the roofs of their townhomes had deteriorated, resulting in impairment of the strength and structural integrity of the roofs.<sup>129</sup> The plaintiffs sued the manufacturers of the FRT plywood under negligence and strict liability theories, seeking damages for the expenses of inspecting, repairing, and replacing the roofs.<sup>130</sup> Invoking *Atlantis*, the plaintiffs contended that the condition of the roofs created a risk of personal injury since injury could result from walking on the roofs or from a collapse of the roofs, although no personal injuries had yet occurred.<sup>131</sup>

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125. *Id.* at 252, 634 A.2d at 1333.

126. *Id.* at 253, 634 A.2d at 1334. The only other reported decision in Maryland in which there was damage to "other property" is *Worm v. American Cyanamid Co.*, 20 U.C.C. Rep. Serv. 2d (Callaghan) 441 (D. Md. 1992), *aff'd*, 5 F.3d 774 (4th Cir. 1993). In *Worm*, three commercial farmers sued the manufacturer of "Scepter," a herbicide, for damages sustained to their corn crop. *Id.* at 441. The farmers had used the herbicide successfully in a prior harvest of soybeans. *Id.* After the soybean harvest, the farmers planted corn on 74 acres of land that had previously been treated with Scepter. *Id.* When the corn crop failed to meet commercial standards for sale, the farmers sued the manufacturer for negligently failing to test Scepter and negligently failing to properly formulate and manufacture the product. *Id.* at 442.

Applying Maryland law, the district court acknowledged that the Court of Appeals of Maryland had not definitively resolved the issue, first broached in *Atlantis* and *Jacques*, whether, in the absence of privity, Maryland recognizes negligence actions when no personal injury damages are claimed. *Id.* The district court refused to "needlessly anticipate the development of state tort law," and concluded that, whatever the result of this inquiry, the plaintiff farmers had not generated sufficient issues of fact to withstand the manufacturer's motion for summary judgment. *Id.*

127. *A.J. Decoster*, 333 Md. at 250-51, 634 A.2d at 1332.

128. 99 Md. App. 646, 639 A.2d 147, *cert. granted*, 336 Md. 98, 646 A.2d 1018 (1994).

129. *Id.* at 650, 639 A.2d at 150.

130. *Id.*

131. *Id.* at 655-56, 639 A.2d at 152.

The court was quick to distinguish the plaintiffs' damages from those alleged in *Atlantis*, noting that "this is not a case where a sudden fire could reasonably be calculated to result in serious physical injury or death in addition to property damage."<sup>132</sup> Rather, the court found that the damage to the roofs was qualitative in nature because it occurred through gradual deterioration of the plywood.<sup>133</sup> The plaintiffs alleged only that the plywood had "darkened, spotted, warped and fractured."<sup>134</sup> Thus, the court found that the damage to the FRT plywood fell short of creating a clear danger of death or personal injury.<sup>135</sup> The court upheld the lower court's dismissal of the plaintiffs' negligence count on the basis that they had alleged in merely "conclusory terms" that someone could be hurt if they were walking on the roof, or if a heavy snowfall occurred triggering a collapse.<sup>136</sup> "Mere possibilities," the court held, "do not meet the threshold of establishing a clear danger of death or personal injury."<sup>137</sup>

The United States District Court for the District of Maryland applied *Atlantis* in one decision, but denied recovery against the defendant manufacturer because its defective product had not presented a risk of personal injury to the purchaser of the product or others. In *In re Lone Star Industries, Inc., Concrete Railroad Cross Ties Litigation*,<sup>138</sup> the district court found that premature cracking and deterioration of concrete railroad ties purchased by the plaintiff, Amtrak, did not pose a "clear danger of death or personal injury."<sup>139</sup> By the plaintiff's own admission, only 6.8% of the ties had lost some of their load bearing capacity and needed to be replaced.<sup>140</sup> The court found that the danger of the ties failing and causing a derailment or other calamitous event was "merely speculative at best

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132. *Id.* at 655, 639 A.2d at 152.

133. *Id.*

134. *Id.*

135. *Id.* The plaintiffs had owned their townhouses for six to ten years and had yet to replace the roofs for fear of personal injury. *Id.* at 655, 639 A.2d at 152.

136. *Id.* at 655, 639 A.2d at 152.

137. *Id.* at 655-56, 639 A.2d at 152. One inevitable result of the *Atlantis* decision has been that in support of their negligence claims, plaintiffs typically allege in their complaint as a matter of course that the defendant's negligence created a risk of personal injury. The court's holding in *Morris* indicates that it will not involve itself in the business of rubber stamping complaints and denying motions to dismiss and motions for summary judgment merely because a plaintiff has perfunctorily alleged in the complaint that a risk of personal injury exists.

138. 776 F. Supp. 206 (D. Md. 1991).

139. *Id.* at 222.

140. *Id.*

and [was] not the type of circumstance which would support the assertion of a tort claim."<sup>141</sup>

Prior to these decisions, the Maryland courts had never before applied the "risk of harm" approach in a products liability suit. The few decisions by the state's courts that addressed the economic loss doctrine generally followed the majority approach in the country—permitting recovery under a negligence theory only where the harm resulting from a defective product was in the form of personal injury or damage to "other property."<sup>142</sup> Whenever injury to the product itself was incurred, such as qualitative defects in the product or losses that were purely pecuniary in nature, Maryland courts invariably denied recovery in tort by a third party.<sup>143</sup> For example, in *Excavation Construction, Inc. v. Mack Trucks, Inc.*,<sup>144</sup> a construction company sued the manufacturer of defective dump trucks in negligence and for breach of the implied warranty of merchantability.<sup>145</sup> The plaintiff claimed as damages the financial losses incurred when the trucks were idle for a period of time.<sup>146</sup> The district court held that the defendant was entitled to summary judgment on the negligence count, finding that the Maryland courts would not extend a manufacturer's liability to that type of economic injury.<sup>147</sup>

Interestingly, the court indicated that it would recognize a distinction between two types of harm that may occur "to the product itself"—physical damage to the product and pecuniary loss without physical harm to the product.<sup>148</sup> The court quoted with approval an oft-cited passage from Dean Prosser:

There can be no doubt that the seller's liability for negligence covers any kind of physical harm, including not only personal injuries, *but also property damage to the defective chattel itself*, . . . as well as damage to other property in the vicinity. But where there is no accident, and no physical damage, and the only loss is a pecuniary one, through the

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141. *Id.* at 223.

142. *See, e.g.,* *Worm v. American Cyanamid Co.*, 20 U.C.C. Rep. Serv. (Callaghan) 441 (D. Md. 1992), *aff'd*, 5 F.3d 774 (4th Cir. 1993) (granting defendant manufacturer's motion for summary judgment on tort claims brought for damages to "other property").

143. *See In re Lone Star Indus., Inc., Concrete R.R. Cross Ties Litig.*, 776 F. Supp. 206 (D. Md. 1991); *Wood Prods., Inc. v. CMI Corp.*, 651 F. Supp. 641 (D. Md. 1986); *Copiers Typewriters Calculators, Inc. v. Toshiba Corp.*, 576 F. Supp. 312 (D. Md. 1983); *Excavation Constr., Inc. v. Mack Trucks, Inc.*, 31 U.C.C. Rep. Serv. (Callaghan) 1386 (D. Md. 1981).

144. 31 U.C.C. Rep. Serv. (Callaghan) 1386 (D. Md. 1981).

145. *Id.* at 1387.

146. *Id.*

147. *Id.* at 1391-92.

148. *Id.* at 1390-91.

loss of the value or use of the thing sold, or the cost of repairing it, the courts have adhered to the rule . . . that purely economic interests are not entitled to protection against mere negligence, and so have denied recovery.<sup>149</sup>

Thus, the court implied that it would hold a manufacturer liable in negligence if there was harm to the product that was physical in nature, but would not hold the manufacturer liable if the plaintiff suffered purely pecuniary losses.<sup>150</sup> The plaintiff in *Excavation Construction* was clearly seeking damages from this latter category by bringing suit for lost profits incurred as a result of the idle trucks.<sup>151</sup> Though the decision does not describe the nature of the "defect" afflicting the trucks, the court apparently concluded that no physical damage had occurred to the trucks themselves.

In addition to purely pecuniary losses, the district court has also held that qualitative defects in a product, such as those incurred in *Morris*, are not recoverable in a negligence action against a manufacturer. In *Wood Products, Inc. v. CMI Corp.*,<sup>152</sup> the plaintiff had purchased a wood furnace from the defendant manufacturer for use in its milling business.<sup>153</sup> Shortly after the furnace was installed, problems developed as a result of defects in its design and manufacture.<sup>154</sup> The evidence presented to the court revealed that the drum of the furnace was "too thin" and "too flexible"; the air distribution tubes "sagged and failed"; the seals of the furnace "were of a lesser quality than had been promised"; only one of several thermocouples "ever worked satisfactorily"; and temperatures within the furnace "were frequently excessive."<sup>155</sup> The furnace simply "never [had] and

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149. *Id.* at 1391 (citing KEETON ET AL., *supra* note 14, § 101, at 665) (emphasis added). In the fifth edition of his treatise, Prosser takes a decidedly different view of when damage to the property itself is recompensable:

Making liability depend upon whether or not the loss results from an "accident" creates a difficult issue and arguably an irrelevant issue with respect to the validity of contract provisions allocating the risk of loss for harm to the defective product itself to the purchaser. Distinguishing "accidental" damage to the product from mere economic loss is difficult in many cases.

KEETON ET AL., *supra* note 14, § 101(3), at 709.

150. In the passage quoted by the court, Dean Prosser indicates that some "accident" to the chattel is required in a negligence action against the manufacturer. Whether this is a reference to the "sudden and calamitous" exception is unclear. Arguably, any type of physical harm to a product is an accident, even where it does not occur in a sudden and calamitous manner.

151. *Excavation Construction*, 31 U.C.C. Rep. Serv. (Callaghan) at 1387.

152. 651 F. Supp. 641 (D. Md. 1986).

153. *Id.* at 644.

154. *Id.* at 646.

155. *Id.*

never [would] work.”<sup>156</sup> The court stated that it “doubt[ed] that the furnace could ever have functioned for its intended purpose.”<sup>157</sup> The court dismissed the plaintiff’s negligence claim against the manufacturer on the ground that the plaintiff alleged only damages for economic loss,<sup>158</sup> although it failed to discuss why the harm to the furnace was characterized as such. It is apparent, however, that the defects and deficiencies in the furnace were of a qualitative nature, rather than the result of physical harm to property—either “other property” or the product itself. Warranty law therefore provided the appropriate remedy.

Thus, *Morris*, *Excavation Construction*, and *Wood Products* indicate that there are two instances under Maryland law in which a plaintiff may not recover economic losses in a negligence action: (1) when purely pecuniary harm has been incurred, or (2) when the damage to the product is merely qualitative in nature and not in the form of actual physical harm. When the harm incurred to the product falls into either category, the policy reasons supporting the application of the economic loss doctrine are perhaps at their strongest.<sup>159</sup> The risk that a purchaser of a product might sustain purely pecuniary injury, such as lost profits, is a risk that typically is, or should be, assumed by a contract between the parties. Likewise, qualitative deficiencies in a product, such as those incurred in *Wood Products* and *Morris*, are the type of harm that statutory warranties are designed to remedy. A manufacturer, it is argued, “does not assume responsibility for the commercial viability or economic performance of the item sold.”<sup>160</sup> As the court of appeals stated in *A.J. Decoster*:

The distinction between tort recovery for physical injury and warranty recovery for economic loss derives from policy considerations which allocate the risks related to a defective product between the seller and the purchaser. A manufacturer may be held liable for physical injuries, including harm to property, caused by defects in its products because it is charged with the responsibility of ensuring that its products meet a standard of safety creating no unreasonable risk of harm. However, where the loss is purely economic, the manufacturer cannot be charged with the responsibility of ensuring that the product meet the particular expectations of the consumer unless it is aware of those expectations and

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156. *Id.*

157. *Id.*

158. *Id.* at 648.

159. See *supra* notes 26-36 and accompanying text.

160. *Berg v. General Motors Corp.*, 555 P.2d 818, 819 (Wash. 1976), *superseded* by WASH. REV. CODE § 7.72 *et seq.* (1993).

has agreed that the product will meet them. Thus, generally, the only recovery for a purely economic loss would be under a contract theory.<sup>161</sup>

*D. Recovery of Economic Loss Against Manufacturers Under Other Causes of Action—Strict Liability, Negligent Misrepresentation, and Breach of Express and Implied Warranties*<sup>162</sup>

Alternative theories under which a plaintiff might attempt to recover economic losses against a manufacturer in the absence of privity include strict liability, negligent misrepresentation, and breach of warranty. The Court of Special Appeals of Maryland has indicated that these theories are not duplicative and, therefore, may be brought as independent, parallel bases of recovery.<sup>163</sup>

The Court of Appeals of Maryland, in *Phipps v. General Motors Corp.*,<sup>164</sup> adopted the theory of strict liability set forth in section 402A of the Restatement (Second) of Torts, which expressly rejects the privity requirement when a party sues a manufacturer in strict liability.<sup>165</sup> Section 402A provides:

(1) One who sells any product in a defective condition unreasonably dangerous to the user or consumer or to his property is subject to liability for physical harm thereby

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161. 333 Md. 245, 250-51, 634 A.2d 1330, 1332-33 (1994).

162. This Comment provides only cursory coverage of the economic loss rule under causes of action other than negligence.

163. *Dechello v. Johnson Enters.*, 74 Md. App. 228, 235 n.4, 536 A.2d 1203, 1207 n.4, *cert. denied*, 312 Md. 601, 541 A.2d 964 (1988); *Valk Mfg. Co. v. Rangaswamy*, 74 Md. App. 304, 310, 537 A.2d 622, 625 (1988), *rev'd en banc*, *Montgomery City v. Valk Mfg. Co.*, 317 Md. 185, 562 A.2d 1246 (1989).

164. 278 Md. 337, 353, 363 A.2d 955, 963 (1976). In *Phipps*, Judge Eldridge explained the following reasons for imposing strict liability on manufacturers: (1) manufacturers are better able financially to bear the risk of loss, (2) consumers rely on manufacturers in expecting that the products they purchase will be safe for their intended purposes, and that this expectation is better met by strict liability than negligence, and (3) the requirement that the defect in a product render it unreasonably dangerous is a sufficient showing of fault to warrant imposing liability. *Id.* at 343, 363 A.2d at 958.

165. For a plaintiff to recover under strict liability, it must be established that: (1) the product was in defective condition at the time it left the possession or control of the seller, (2) the product was unreasonably dangerous to the user or consumer, (3) the defect in the product was the cause of the plaintiff's injuries, and (4) the product was expected to and did reach the consumer without substantial change in its condition. *Kelley v. R.G. Indus., Inc.*, 304 Md. 124, 134, 497 A.2d 1143, 1147 (1985) (*citing Phipps v. General Motors Corp.*, 278 Md. 337, 363 A.2d 955 (1976)); *Ellsworth v. Sherne Lingerie, Inc.*, 303 Md. 581, 495 A.2d 348 (1985); *Sheehan v. Anthony Pools*, 50 Md. App. 614, 440 A.2d 1085 (1982), *aff'd*, 295 Md. 285, 455 A.2d 434 (1983).



caused to the ultimate user or consumer, or to his property, if

(a) the seller is engaged in the business of selling such a product, and

(b) it is expected to and does reach the user or consumer without substantial change in the condition in which it is sold.

(2) The rule stated in Subsection (1) applies although

(a) the seller has exercised all possible care in the preparation and sale of his product, and

(b) *the user or consumer has not bought the product from or entered into any contractual relation with the seller.*<sup>166</sup>

Section 402A(2)(b) grants the right of recovery to both the "user"<sup>167</sup> and "consumer"<sup>168</sup> of a product, despite their lack of privity because neither person purchased the product directly from the manufacturer. In fact, the court of special appeals has determined that the scope of liability under the terms "user" and "consumer" extends to even mere "bystanders."<sup>169</sup>

166. RESTATEMENT (SECOND) OF TORTS § 402A (1964) (emphasis added). The Maryland courts have also adopted the theory, similar to that set forth in § 402A, that "privity is not required to maintain a suit against a manufacturer or seller for an injury sustained in the use of a chattel *which is likely to be dangerous for the use for which it was supplied.*" *Uppgren v. Executive Aviation Servs., Inc.*, 326 F. Supp. 709, 716-17 (D. Md. 1971) (emphasis added). This theory is set forth in § 388 of the Restatement, which provides as follows:

**Chattel Known to be Dangerous for Intended Use**

One who supplies directly or through a third person a chattel for another to use is subject to liability to those whom the supplier should expect to use the chattel with the consent of the other or to be endangered by its probable use, for physical harm caused by the use of the chattel in the manner for which and by a person for whose use it is supplied, if the supplier

(a) knows or has reason to know that the chattel is likely to be dangerous for the use for which it is supplied, and

(b) has reason to believe that those for whose use the chattel is supplied will realize its dangerous condition, and

(c) fails to exercise reasonable care to inform them of its dangerous condition or of the facts which make it likely to be dangerous.

RESTATEMENT (SECOND) OF TORTS § 388 (1964); *see also* *Excavation Constr., Inc. v. Mack Trucks, Inc.*, 31 U.C.C. Rep. Serv. (Callaghan) 1386 (D. Md. 1981); *Babylon v. Scruton*, 215 Md. 299, 138 A.2d 375 (1958); *Kaplan v. Stein*, 198 Md. 414, 84 A.2d 81 (1951).

167. A "user" is defined in comment 1 as a person who passively enjoys the benefit of the product. RESTATEMENT (SECOND) OF TORTS § 402A cmt. 1 (1964).

168. A "consumer" is defined as one who purchases a product or who is a member of the family of the final purchaser, his employee, his guest, or a donee of the purchaser. *Id.*

169. *Valk Mfg. Co. v. Rangaswamy*, 74 Md. App. 304, 323, 537 A.2d 622, 627

In *Phipps*, the court of appeals applied the strict liability theory in a case involving personal injuries caused by a defective product.<sup>170</sup> The court held that the plaintiff, who was injured when the car he was driving suddenly accelerated and crashed into a tree, had stated a cause of action under section 402A against the manufacturer of the car despite the lack of privity.<sup>171</sup>

The Maryland courts have not applied section 402A to allow a plaintiff to recover purely economic loss in the form of either pecuniary losses or qualitative defects in a product. In those few decisions that have addressed the issue, the courts have held that such claims cannot be brought under either a strict liability or a negligence theory.<sup>172</sup> In *A.J. Decoster*, however, application of section 402A was extended for the first time to damage other than personal injury.<sup>173</sup> The plaintiff in *A.J. Decoster*, in addition to a negligence claim, also brought a strict liability claim for the death of its chickens, which the court characterized as damage to "other property."<sup>174</sup> In its motion to dismiss the strict liability count, the defendant argued that the legislature's enactment of warranty remedies under the UCC created a comprehensive scheme of recovery for economic losses that preempted the field of products liability.<sup>175</sup> Relying on *Phipps* and a literal reading of section 402A,<sup>176</sup> the court

(1988), *rev'd en banc*, *Montgomery City v. Valk Mfg. Co.*, 317 Md. 185, 562 A.2d 1246 (1989). Most other jurisdictions in the country provide relief to bystanders under § 402A. *Id.* at 322-33, 537 A.2d at 629-32.

170. *Phipps v. General Motors Corp.*, 278 Md. 307, 353, 363 A.2d 955, 963 (1976).

171. *Id.*

172. *In re Lone Star Indus., Inc., Concrete R.R. Cross Ties Litig.*, 776 F. Supp. 206, 221-22 (D. Md. 1991) (characterizing deterioration damage to railroad ties as economic loss and denying recovery of such loss in negligence and strict liability action against the manufacturer of ties); *Copiers Typewriters Calculators, Inc. v. Toshiba Corp.*, 576 F. Supp. 312, 325-26 (D. Md. 1983) (denying recovery of economic losses in both strict liability and negligence, without distinguishing the two theories).

The United States Supreme Court has likewise held that a products liability claim, whether based on a theory of negligence or strict liability, cannot be asserted when the only injury claimed is purely economic loss. *East River S.S. Corp. v. Transamerica Delaval, Inc.*, 476 U.S. 858 (1986). See *supra* parts III.A-B. This is generally the approach taken by most states in the country. For a discussion of this approach and the minority approach, which holds that purely economic losses are recoverable in strict liability, see Joe E. Manuel & Gregory B. Richards, *Economic Loss in Strict Liability—Beyond the Realm of 402A*, 16 MEM. ST. U. L. REV. 315 (1986).

173. 333 Md. 245, 258, 634 A.2d 1330, 1336 (1994).

174. *Id.* at 253, 634 A.2d at 1332.

175. *Id.* at 255, 634 A.2d at 1334-35.

176. The court noted that § 402A(1) describes the applicable seller as "[o]ne who sells any product in a defective condition unreasonably dangerous to the user or consumer or to his property" and further provides that a seller is liable for "physical harm thereby caused to the ultimate user or consumer or his property." *Id.* at 258, 634 A.2d at 1336.

of appeals rejected the defendant's preemption argument and held that "[i]t is beyond question that § 402A applies not only to accidental injuries to consumers or users of a product, but also to injury to the property of the user or consumer."<sup>177</sup> The court based its holding primarily on equitable principles, reasoning that fairness required recovery for injuries to person *and* property resulting from unreasonably dangerous conditions.<sup>178</sup> A consumer, the court stated, does not simply lose the benefit of his bargain when a product proves defective, but rather sustains damage to other property because the defect is so dangerous in nature.<sup>179</sup> The court concluded that a consumer does not "bargain[] for destruction of his property any more than he should be considered to have bargained for physical injury to himself or others."<sup>180</sup>

In negligent misrepresentation actions,<sup>181</sup> the Maryland courts have permitted recovery of economic losses only in certain instances.<sup>182</sup> The courts have, for example, allowed (1) a plaintiff to recover against a mortgage broker for economic losses incurred in relying on the broker's advice;<sup>183</sup> (2) a prospective homeowner to recover against a developer for a grossly inaccurate estimate of water and sewer connection charges;<sup>184</sup> and (3) a plaintiff to recover for overpayment of a stock purchase as a result of a brokerage's negligent misrepresentations.<sup>185</sup> The courts have not, however, permitted the recovery of purely economic losses in a products liability setting

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177. *Id.*

178. *Id.* at 259, 634 A.2d at 1337.

179. *Id.*

180. *Id.* at 259-60, 634 A.2d at 1337.

181. The elements of negligent misrepresentation are as follows:

- (1) the defendant, owing a duty of care to the plaintiff, negligently asserts a false statement;
- (2) the defendant intends that his statement will be acted upon by the plaintiff;
- (3) the defendant has knowledge that the plaintiff will probably rely on the statement, which, if erroneous, will cause loss or injury;
- (4) the plaintiff, justifiably, takes action in reliance on the statement; and
- (5) the plaintiff suffers damage proximately caused by the defendant's negligence.

*Weisman v. Connors*, 312 Md. 428, 444, 540 A.2d 783, 791 (1988) (citing *Martens Chevrolet v. Seney*, 292 Md. 328, 337, 439 A.2d 534, 539 (1982)).

182. *See, e.g., St. Paul at Chase Corp. v. Manufacturers Life Ins. Co.*, 262 Md. 192, 278 A.2d 12, *cert. denied*, 404 U.S. 857 (1971); *Brack v. Evans*, 230 Md. 548, 187 A.2d 880 (1963); *Ward Dev. Co. v. Ingrao*, 63 Md. App. 645, 493 A.2d 421 (1985).

183. *See St. Paul*, 262 Md. 192, 278 A.2d 12.

184. *See Ingrao*, 63 Md. App. 645, 493 A.2d 421.

185. *See Brack*, 230 Md. 548, 187 A.2d 880.

based on a negligent misrepresentation theory.<sup>186</sup> Generally, the courts reason that Maryland's "pervasive statutory scheme" governing warranty claims adequately protects plaintiffs against economic losses caused by the misrepresentations of a seller or manufacturer regarding their products.<sup>187</sup>

The Court of Special Appeals of Maryland addressed the applicability of the economic loss doctrine in a negligent misrepresentation action in *Boatel Industries, Inc. v. Hester*.<sup>188</sup> The plaintiffs in *Boatel Industries* purchased a yacht which proved to have a cracked hull and other design and structural defects rendering it unseaworthy.<sup>189</sup> They brought suit against the manufacturer of the yacht for breach of warranty and negligent misrepresentations allegedly made by the manufacturer concerning the construction and seaworthiness of the yacht.<sup>190</sup> The court of special appeals found that the unseaworthy and unsafe condition of the yacht created "a risk of death or personal injury" to plaintiffs.<sup>191</sup> Citing *Atlantis*,<sup>192</sup> the court noted that because the plaintiffs had not incurred physical injuries, their damages were entirely economic in nature.<sup>193</sup> Further, the court noted that under *Atlantis* a claimant need not wait for personal injury to occur before bringing a negligence action.<sup>194</sup> Nevertheless, the court refused to extend *Atlantis* to cases of negligent misrepresentation.<sup>195</sup> The court reasoned that the damages recoverable for negligent misrepresentation—the reasonable cost of correcting the dangerous condition—are "included within the damages recoverable under the warranty counts."<sup>196</sup>

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186. *Flow Indus., Inc. v. Fields Constr. Co.*, 683 F. Supp. 527 (D. Md. 1988); *Wood Prods., Inc. v. CMI Corp.*, 651 F. Supp. 641 (D. Md. 1986); *Copiers Typewriters Calculators v. Toshiba Corp.*, 576 F. Supp. 312 (D. Md. 1983); *Boatel Indus. v. Hester*, 77 Md. App. 284, 550 A.2d 389 (1988).

187. *Wood Prods.*, 651 F. Supp. at 648.

188. 77 Md. App. 284, 550 A.2d 389 (1988).

189. *Id.* Other problems plaguing the vessel included engine and generator malfunctions, air conditioning and heating problems, and an excessive fuel consumption rate. *Id.* at 293, 550 A.2d at 394.

190. *Id.* at 307, 550 A.2d at 397-98.

191. *Id.* at 308, 550 A.2d at 401.

192. 308 Md. 18, 517 A.2d 336 (1986).

193. *Boatel*, 77 Md. App. at 307, 550 A.2d at 401. The court implied that in products liability cases, personal injury is a necessary element of a cause of action for negligent misrepresentation. *Id.* (citing *Weisman v. Connors*, 312 Md. 428, 540 A.2d 783 (1988)).

194. *Id.*

195. *Id.*

196. *Id.*; see also *Wood Prods., Inc. v. CMI Corp.*, 651 F. Supp. 641, 648 (D. Md. 1986) (denying plaintiff's negligent misrepresentation claim against manufacturer for false statements regarding capabilities of and improvements to wood furnace, on basis that "[a] pervasive statutory scheme governs warranty

In claims for breach of the implied warranty of merchantability, the privity requirement has been expressly abolished by the Maryland General Assembly.<sup>197</sup> Protection under this warranty extends not only to a party who purchases the product for resale to a consumer, but also to the ultimate consumer.<sup>198</sup> The plaintiff who brings an action for breach of the implied warranty of merchantability may recover economic losses as "incidental" or "consequential" damages under section 2-715 of the Commercial Law Article of the Maryland Code.<sup>199</sup>

In claims for either breach of the express warranty or breach of the implied warranty of fitness for a particular purpose, the privity requirement has also been expressly eliminated, but only when the

claims in product liability cases, and it appears inappropriate to extend theories of negligent misrepresentation into an area where the General Assembly has carefully determined who may assert what claims against whom").

197. MD. CODE ANN., COM. LAW I § 2-314(1)(a)-(b) (1976). Subsections (a) and (b) of § 2-314(1) provide as follows:

(a) In §§ 2-314 through 2-318 of this title, "seller" includes the manufacturer, distributor, dealer, wholesaler or other middleman or retailer; and

(b) Any previous requirement of privity is abolished as between the buyer and seller in any action brought by the buyer.

*Id.*; see *Copiers Typewriters Calculators, Inc. v. Toshiba Corp.*, 576 F. Supp. 312, 322-23 (D. Md. 1983). Maryland is one of only a few states which has altered the Uniform Commercial Code to expressly abolish the privity requirement. THOMAS M. QUINN, QUINN'S UNIFORM COMMERCIAL CODE COMMENTARY AND LAW DIGEST 2-229 (2d ed. 1991).

198. *Sheeskin v. Giant Food, Inc.*, 20 Md. App. 611, 318 A.2d 874 (1974), *aff'd*, 273 Md. 592, 332 A.2d 1 (1975); *Erdman v. Johnson Bros. Radio & Television Co.*, 260 Md. 190, 271 A.2d 744 (1970).

199. Section 2-715 provides:

(1) Incidental damages resulting from the seller's breach include expenses reasonably incurred in inspection, receipt, transportation and care and custody of goods rightfully rejected, any commercially reasonable charges, expenses or commissions in connection with effecting cover and any other reasonable expense incident to the delay or other breach.

(2) Consequential damages resulting from the seller's breach include  
 (a) Any loss resulting from the general or particular requirements and needs of which the seller at the time of contracting had reason to know and which could not reasonably be prevented by cover or otherwise; and  
 (b) Injury to person or property proximately resulting from any breach of warranty.

MD. CODE ANN., COM. LAW I § 2-715 (1992).

For example, in *Excavation Construction, Inc. v. Mack Trucks, Inc.*, 311 U.C.C. Rep. Serv. (Callaghan) 1386 (D. Md. 1981), the court held that economic losses, in the form of lost profits incurred by the plaintiff while its trucks were idle, were consequential damages within the meaning of § 2-715(2). *Id.* at 1388.

plaintiff has suffered personal injury.<sup>200</sup> When only economic loss is incurred, privity is required in an action brought pursuant to either of these theories.<sup>201</sup>

As *Boatel Industries* indicates, a plaintiff is most likely to recover economic losses in a breach of warranty action brought under Maryland's Commercial Law Article.<sup>202</sup> There are obvious advantages to bringing a breach of warranty claim, the most significant of which is that a plaintiff may recover without proving negligence on the part of the manufacturer or seller.<sup>203</sup> The plaintiff need only demonstrate the existence of the warranty, a breach of that warranty, and that the breach was the proximate cause of the loss sustained.<sup>204</sup> Any knowledge of the defect by the manufacturer or seller, or any lack of care, is irrelevant.<sup>205</sup>

200. Section 2-318 of the Commercial Law Article extends a seller's warranties, whether express or implied,

to any natural person who is in the family or household of his buyer or who is a guest in his home or any other ultimate consumer or user of the goods or person affected thereby if it is reasonable to expect that such person may use, consume or be affected by the goods *and who is injured in person by breach of the warranty.*

MD. CODE ANN., COM. LAW I § 2-318 (1992) (emphasis added).

201. *See Wood Prods., Inc. v. CM1 Corp.*, 651 F. Supp. 641, 649 (D. Md. 1986). In *Wood Products*, the court found that there was privity between the buyer of the defective furnace and the furnace manufacturer, and that the buyer could therefore recover economic losses on a breach of implied warranty of fitness for a particular purpose theory. *Id.* Interestingly, the court also found that even assuming that the parties were not in privity, the manufacturer would still be liable on the warranty claim since it "played a significant role in the sale of the furnace . . . [and] actively solicited and dominated the negotiations." *Id.* The court held that the manufacturer was estopped from denying that it was in privity with the buyer. *Id.* at 649-50 (citing *Addressograph-Multigraph Corp. v. Zink*, 273 Md. 277, 329 A.2d 28 (1974)).

202. MD. CODE ANN., COM. LAW I § 2-313 *et seq.* (1992).

203. *See Sheeskin v. Giant Food, Inc.*, 20 Md. App. 611, 318 A.2d 874 (1974), *aff'd*, 273 Md. 592, 332 A.2d 1 (1975).

204. *Fellows v. USV Pharmaceutical Corp.*, 502 F. Supp. 297, 299 (D. Md. 1980); *Certain-Teed Prods. Corp. v. Goslee Roofing & Sheet Metal, Inc.*, 26 Md. App. 452, 463, 339 A.2d 302, 309 (1975); *Sheeskin v. Giant Food, Inc.*, 20 Md. App. 611, 621, 318 A.2d 874, 880 (1974), *aff'd*, 273 Md. 592, 332 A.2d 1 (1975). In the context of construction defects see *Starfish Condominium Ass'n v. Yorkridge Service Corp.*, 295 Md. 693, 710, 458 A.2d 805, 814 (1983).

205. *Frericks v. General Motors Corp.*, 274 Md. 288, 300, 336 A.2d 118, 126 (1975), *rev'd on other grounds*, 278 Md. 304, 363 A.2d 460 (1976). As the comment to § 2-314 of the Commercial Law Article notes, "an affirmative showing by the seller that the loss resulted from some action or event following his own delivery of the goods can operate as a defense." MD. CODE ANN., COM. LAW I § 2-314 cmt. 13 (1992). Also, a showing by the seller that it exercised care in its manufacture, processing or selection of the product is relevant to whether or not the warranty was in fact breached. *Id.*

On the other hand, there are also clear advantages to bringing a claim for economic loss under a tort theory. For example, warranty liability can be waived through the use of a disclaimer.<sup>206</sup> Although the General Assembly has extinguished the right of sellers to disclaim or limit warranties in the sale of consumer goods,<sup>207</sup> there is no similar limitation with respect to non-consumer goods. In addition, the notice requirements of the UCC may also prove to be an obstacle to recovery.<sup>208</sup> Also, the applicable statute of limitations for a breach of warranty may, through the use of boilerplate language, be reduced to as short as one year.<sup>209</sup>

#### IV. RECOVERY OF ECONOMIC LOSS IN CASES INVOLVING NEGLIGENT DESIGN OR CONSTRUCTION

The tort liability of building contractors to third parties has generally followed the same path of development as that of manufacturers of chattels,<sup>210</sup> although, as Dean Prosser has observed, "[t]his was a field in which the ghost of *Winterbottom v. Wright* died very hard."<sup>211</sup> The privity defense was the major obstacle to imposing a tort duty on building contractors for negligent design or construction.<sup>212</sup> Several other mechanisms also initially shielded contractors from tort liability to third parties. These included the common-law doctrines of *caveat emptor*<sup>213</sup> and "merger by deed,"<sup>214</sup> and

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206. See MD. CODE ANN., COM. LAW I § 2-316 (1992).

207. See MD. CODE ANN., COM. LAW I § 2-316.1 (1992).

208. See MD. CODE ANN., COM. LAW I §§ 2-602, 2-607 (1992). While the court of appeals has held that a third party beneficiary of a seller's warranties is not required to give notice of a breach, the actual purchaser of the product must still do so as a prerequisite to recovery. See generally *Frericks v. General Motors Corp.*, 274 Md. 288, 305-06, 336 A.2d 118, 128 (1975).

209. MD. CODE ANN., COM. LAW I § 2-725(1) (1992).

210. F. HARPER ET AL., *supra* note 8, § 18.5, at 705-11.

211. KEETON ET AL., *supra* note 14, § 104A, at 722 (citing 152 Eng. Rep. 402 (1842)).

212. See generally *Barrett*, *supra* note 12, at 903-05.

213. *Id.* The doctrine of *caveat emptor*, or "buyer beware," barred a purchaser of a new home from suing the seller for defects in the home, irrespective of what type of damages were incurred—personal injury, property damage, or merely economic loss. See *Leider*, *supra* note 3, at 947; see also *Roberts*, *The Case of the Unwary Buyer: The Housing Merchant Did It*, 52 CORNELL L.Q. 835, 836-37 (1967).

214. The "merger by deed" doctrine provided that the builder's obligations under its contract were "merged" into the deed at closing and were thereby satisfied. See *Barrett*, *supra* note 12, at 904; see also *Millison v. Fruchtmann*, 214 Md. 515, 518, 136 A.2d 240, 242 (1957) (holding that under Maryland law the acceptance of a deed gives rise to prima facie presumption that it is an execution of the entire contract of sale and that the rights of the parties are to be determined by the deed); *Gilbert Constr. Co. v. Gross*, 212 Md. 402, 129 A.2d 518 (1957).

the "completed and accepted" defense.<sup>215</sup>

A. *The Liability of Building Contractors to Third Parties*

As in the case of defective chattels, the traditional rule was that a contractor owed no tort duty to the general public, including the purchaser of the home.<sup>216</sup> The contractor owed a duty only to the developer or general contractor with whom it had privity.<sup>217</sup> In determining whether a tort duty might extend to third parties, an early line of Maryland cases drew a distinction between two types of negligent conduct: (1) non-performance of a contractual duty, or "nonfeasance", and (2) improper performance of a contractual duty, or "misfeasance."<sup>218</sup> Where a contractor simply did nothing to perform a contractual duty—nonfeasance—it was held that the contractor could be held liable only to the party to whom contractual duties were owed.<sup>219</sup> On the other hand, where a contractor performed a contractual duty but did so improperly—misfeasance—it was held that the contractor could be held liable to third parties as well.<sup>220</sup>

One of the most frequently cited of these early cases is *Marlboro Shirt Co. v. American District Telegraph Co.*,<sup>221</sup> The plaintiff in *Marlboro Shirt* was a tenant in a building whose owner was under contract with the defendant, a telegraph company, to install an "automatic central station signaling device" in the building's sprinkler system.<sup>222</sup> In the event of a water leakage in the sprinkler system, the device was intended to send a signal to the office of the defendant, who would then notify the proper authorities.<sup>223</sup> The sprinkler system soon developed a leak which was not detected by the defendant's device and not reported to the telegraph company's office, resulting

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215. Under the "completed and accepted" defense, once construction was completed and the work was accepted by the owner, the builder could not be held liable to anyone except the owner. See generally Annotation, *Negligence of Building or Construction Contractor as Condition of Liability upon His Part for Injury or Damage to Third Party Occurring After Completion and Acceptance of Work*, 58 A.L.R.2d 865 (1958).

216. See *Huset v. J.I. Case Threshing Mach. Co.*, 120 F. 865, 867-68 (8th Cir. 1903).

217. See *id.* at 867.

218. *Marlboro Shirt Co., Inc. v. American Dist. Tel. Co.*, 196 Md. 565, 77 A.2d 776 (1950); *East Coast Freight Lines, Inc. v. Consolidated Gas, Electric Light & Power Co.*, 187 Md. 385, 50 A.2d 246 (1946); *Consolidated Gas, Electric Light & Power Co. v. Connor*, 114 Md. 140, 78 A. 725 (1910).

219. *East Coast Freight Lines*, 187 Md. at 402-03, 50 A.2d at 254.

220. *Consolidated Gas Co.*, 114 Md. at 156-57, 78 A. at 729; see KEETON ET AL., *supra* note 14, § 93, at 670-71.

221. 196 Md. 565, 77 A.2d 776 (1951).

222. *Id.* at 568, 77 A.2d at 776-77.

223. *Id.*



in damage to the plaintiff's personal property.<sup>224</sup> In its negligence action against the telegraph company, the plaintiff did not allege that the company caused the leak, but rather that it failed to detect and report the leak.<sup>225</sup> The case was therefore one of nonfeasance rather than misfeasance. The court of appeals upheld the telegraph company's demurrer, holding that "a contractor owes no duty to the general public for which it may be responsible in an action in tort for negligence, *if it does not perform its contract*. The duty under such contract is only to the one with which the contract is made."<sup>226</sup>

One year after the *Marlboro Shirt* decision, the court of appeals abandoned the misfeasance-nonfeasance distinction in the case of *Otis Elevator Co. v. Embert*.<sup>227</sup> In *Otis Elevator*, the plaintiff brought a negligence action against an elevator maintenance contractor who was under contract with the building owner to maintain the elevator.<sup>228</sup> The plaintiff was not injured by any mechanical defect in the elevator or any failure on the part of the defendant to keep the elevator in repair.<sup>229</sup> Rather, the plaintiff alleged that the elevator company was negligent because when the plaintiff entered the elevator, it was not level thereby causing the plaintiff to fall twelve and one-half inches.<sup>230</sup> In defending the claim, the contractor argued that it owed no duty to the plaintiff to perform its contract with the building company.<sup>231</sup>

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224. *Id.*

225. *Id.* at 568-69, 77 A.2d at 777.

226. *Id.* at 571-72, 77 A.2d at 778 (emphasis added); *accord* East Coast Freight Lines v. Consolidated Gas, Electric Light & Power Co., 187 Md. 385, 50 A.2d 246 (1946) (holding that defendant gas company's failure to perform necessary repairs and replacements to public lighting system pursuant to contract with Baltimore City was nonfeasance, and that plaintiffs, who were not parties to the contract, could not recover against gas company in negligence).

This quotation from *Marlboro Shirt* is often misunderstood and interpreted overbroadly to mean that a contractor can never be held liable in negligence to a third party when that negligence arises out of a contractual obligation. *See* Council of Co-Owners Atlantis Condominium, Inc. v. Whiting-Turner Contracting Co., 308 Md. 18, 29-31, 517 A.2d 336, 342-43 (1986). In fact, the trial judge in *Atlantis*, in upholding the demurrers of the defendants, stated that he was bound by this statement in *Marlboro Shirt* and concluded that Maryland law would not recognize a tort duty in the absence of privity under the circumstances. *Id.* at 24, 517 A.2d at 339. The court of appeals in *Atlantis* disagreed and refused to reaffirm the rather stringent holding of *Marlboro Shirt*, finding that *Marlboro's* general statement "was broader than required for the determination of that case." *Id.* at 30, 517 A.2d at 342.

227. 198 Md. 585, 84 A.2d 876 (1951).

228. *Id.* at 587, 84 A.2d at 876-77. Otis-Elevator was impleaded as a third-party defendant by the building owner who was sued by a passenger. *Id.*

229. *Id.* at 595, 84 A.2d at 880.

230. *Id.* at 593, 84 A.2d at 879.

231. *Id.* at 597, 84 A.2d at 881.

The court first noted that the distinction between misfeasance and nonfeasance "denotes a difference between absence and existence of tort liability, but does not appreciably aid in determining whether or not such liability exists."<sup>232</sup> The court stated further that

[t]he absence of tort liability for breach of contract is not qualified by the distinction between non-feasance and misfeasance. In such cases such a distinction is not between non-performance and 'misperformance' of a contract, but only between conduct, in breach of a contract, which constitutes only a breach of a contract and conduct which also constitutes a breach of duty, arising out of the nature of the work undertaken and the conduct, to third persons.<sup>233</sup>

Because the elevator company had not breached its contract with the building owner, the court looked to the scope of the elevator company's undertaking apart from its contract with the owner.<sup>234</sup> The court cited with apparent approval *MacPherson v. Buick Motor Co.*<sup>235</sup> for the proposition that "the duty to safeguard life and limb" does not grow out of contract and nothing else, but rather "its source [is] in the law."<sup>236</sup> In determining whether the elevator company owed a tort duty independent of the contract, the court held that because the defendant had undertaken responsibility only for the maintenance and not the operation of the elevator, the defendant did not owe a tort duty to the plaintiff.<sup>237</sup>

The *Otis Elevator* decision marked a turning point in Maryland law. The approach taken by the courts thereafter began to focus not on the "archaic distinction"<sup>238</sup> between non-feasance and misfeasance, but rather on the determination of whether a duty was imposed on a defendant to third parties independent of any obligations arising out of its contract.<sup>239</sup> A tort duty owed to third parties, independent

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232. *Id.* at 598, 84 A.2d at 882.

233. *Id.* at 597-98, 84 A.2d at 881.

234. *Id.* at 600-01, 84 A.2d at 883. The court stated that *MacPherson* "has never been expressly approved or disapproved by this court, but has been quoted and distinguished. . . . For present purposes we shall assume that *MacPherson v. Buick Motor Company* and the cases which anticipated or followed it are law in Maryland." *Id.* at 599, 84 A.2d at 882.

235. 111 N.E. 1050 (N.Y. 1916).

236. *Otis Elevator*, 198 Md. at 598, 84 A.2d at 882 (citing *MacPherson*, 111 N.E. at 1053).

237. *Id.* at 601, 84 A.2d at 883.

238. *Matyas v. Suburban Trust Co.*, 257 Md. 339, 343, 263 A.2d 16, 18 (1970).

239. *See, e.g., id.* at 344, 263 A.2d at 19 (holding that "absent a duty exterior to the contract . . . the mere failure to perform does not provide a foundation for an actionable tort"); *Heckrotte v. Riddle*, 224 Md. 591, 595, 168 A.2d 879, 882 (1961) (holding that "[t]he mere negligent breach of a contract, absent a duty or obligation imposed by law independent of that arising out of the contract itself, is not enough to sustain an action sounding in tort").

of contractual obligations, may have its source in "contract, conduct or law."<sup>240</sup> For example, in *Matyas v. Suburban Trust Co.*,<sup>241</sup> the court of appeals found that a shopping center tenant whose lease agreement with the landlord required it to maintain the sidewalk free of ice and snow, did not owe a tort duty "in law" to members of the general public who might slip and fall on the sidewalk.<sup>242</sup> The court noted that no ordinance required property owners to keep public sidewalks abutting their property free of ice and snow.<sup>243</sup> Absent a duty imposed by law and "exterior to the contract" to keep the sidewalks clean, the lessor's failure to do so was not actionable in tort.<sup>244</sup>

In *Cutlip v. Lucky Stores, Inc.*,<sup>245</sup> the court of special appeals indicated that a contractor may owe a tort duty to third parties when it assumes a supervisory role in performing its contract. In *Cutlip*, the plaintiffs' decedent, an iron worker, was killed when a portion of the building he was working on collapsed.<sup>246</sup> The plaintiffs sued the architect, who was under contract with the owner of the property, for negligence on the novel theory that an architect's liability may extend to third parties when he has assumed additional supervisory responsibilities arising from his contract with the owner.<sup>247</sup> The architect's additional supervisory responsibilities in *Cutlip* arose from his agreement to provide Prince George's County with a field inspection report for the property, in order to procure the building permit required by the architect's contract with the owner.<sup>248</sup> The court in *Cutlip* did not decide whether the liability of an architect extends in all cases to the public,<sup>249</sup> but did find that in circumstances where an architect retains supervision of construction and takes on additional supervisory responsibilities, he owes a duty to the general public, including the builder's employees, to ensure safe construction.<sup>250</sup> The court was not entirely clear whether this duty arose out of the contract or by operation of law. The court stated, however, that the architect's "contract with the county to assume additional

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240. *Kreiger v. J.E. Greiner Co., Inc.*, 282 Md. 50, 57, 382 A.2d 1069, 1073 (1978).

241. 257 Md. 339, 263 A.2d 16 (1970).

242. *Id.* at 344, 263 A.2d at 19.

243. *Id.* at 341, 263 A.2d at 17.

244. *Id.* at 344, 263 A.2d at 19.

245. 22 Md. App. 673, 325 A.2d 432 (1974).

246. *Id.* at 676, 325 A.2d at 434.

247. *Id.* at 686-87, 325 A.2d at 440.

248. *Id.*

249. *Id.* at 694-96, 325 A.2d at 444. The court noted that other jurisdictions have recognized this general tort duty on the part of architects. *Id.* at 693, 325 A.2d at 443 (citing *Erhart v. Hummonds*, 334 S.W.2d 869 (Ark. 1960)).

250. *Id.* at 693-95, 325 A.2d at 443-44.

supervisory responsibilities clearly subjected him to a duty which encompassed the decedent."<sup>251</sup>

In *Kreiger v. J.E. Greiner Co.*,<sup>252</sup> decided shortly after *Cutlip*, the court of appeals addressed the liability of supervisory engineers. The plaintiff in *Kreiger* was injured while working on the construction of a bridge.<sup>253</sup> He sued the project's engineers, who were under contract with the State Roads Commission to design the bridge and provide overall supervision of its construction.<sup>254</sup> The court noted that "[i]t is elementary that for there to be liability on the part of these engineers such liability would have to arise by virtue of a duty *under contract, conduct, or law.*"<sup>255</sup> The court, however, did not confront the question of whether a duty on the part of the engineers arose by operation of law. Instead, it focused upon the language of the engineers' contracts with the state, and found that these contracts did not place upon the engineers a duty to supervise safety in connection with the construction and did not hold them responsible for life and property generally.<sup>256</sup> The duty of the engineers under the contracts was simply "to assure a certain end result, a completed bridge which complie[d] with the plans and specifications."<sup>257</sup>

The plaintiffs also alleged that the engineers had assumed other responsibilities, aside from the contract, for the safety of the workers, including the obligation to stop the work when it "was being performed in a negligent and dangerous manner which was unsafe for the workmen."<sup>258</sup> The court did not address this argument because it found that the engineers' contracts with the state negated the allegation that they were required to supervise the work for safety.<sup>259</sup>

Another potential source of duty for contractors, independent of any contract, is the building code. In *Gardenvillage Realty Corp. v. Russo*,<sup>260</sup> a tenant and her mother sued the owner of their residence,

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251. *Id.* at 694, 325 A.2d at 444.

252. 282 Md. 50, 382 A.2d 1069 (1978).

253. *Id.* at 52, 382 A.2d 1070.

254. *Id.*

255. *Id.* at 56-57, 382 A.2d at 1073 (emphasis added). How elementary this proposition was at the time this case was decided is questionable. Notably, the court cited no cases in support of this statement.

256. *Id.* at 68-69, 382 A.2d at 1079.

257. *Id.* at 69, 382 A.2d at 1079.

258. *Id.* at 69-70, 382 A.2d at 1079.

259. *Id.* at 70, 382 A.2d at 1080. The concurring opinion argued that the complaint alleged facts sufficient to establish a cause of action against the engineers on the theory that they voluntarily assumed and then breached a duty of care owed to the plaintiff, independent of any contractual obligations undertaken in their contract with the state. *Id.* at 70-71, 382 A.2d at 1080.

260. 34 Md. App. 25, 366 A.2d 101 (1976).

the general contractor, and others for personal injuries when a concrete slab porch collapsed at their residence.<sup>261</sup> The evidence revealed that the concrete slab was latently defective and not constructed in accordance with the Baltimore City Building Code.<sup>262</sup> The court found that the building code imposed a "non-delegable, affirmative duty" upon the owner to insure compliance with the code.<sup>263</sup>

In 1986, the court of appeals took a decidedly different approach to the determination of whether a contractor owes a tort duty to third parties. In *Council of Co-Owners Atlantis Condominium, Inc. v. Whiting-Turner Contracting Co.*,<sup>264</sup> the court reviewed decisions in both Maryland and other jurisdictions,<sup>265</sup> and determined for the first time that "privity is not an absolute prerequisite to the existence of a tort duty."<sup>266</sup> Rather, the court found that the issue of whether a contractor's tort duty extends to third parties should be resolved by the traditional negligence standard of foreseeability.<sup>267</sup>

Perhaps the death knell to the privity defense was struck in *St. James Construction Co. v. Morlock*.<sup>268</sup> The court of special appeals in *St. James* held that corporate officers and employees of a building contractor can be held personally liable for economic loss, despite the lack of privity with the homeowner.<sup>269</sup> The court refused to recognize "subordinate tiers of privity between corporate 'builders' and their officers and employees."<sup>270</sup> Rather, the court found that the general rule holding corporate agents personally liable for their active participation in corporate torts should apply in actions brought under *Atlantis*.<sup>271</sup> The court reasoned that the *Atlantis* decision sought to allocate risks to those best able to avoid such risks by "substituting foreseeability for contractual privity as the principal determinant of duty."<sup>272</sup>

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261. *Id.* at 26-27, 366 A.2d at 103.

262. *Id.* at 28, 366 A.2d at 104.

263. *Id.* at 39, 336 A.2d at 110. The violation of a building code does not, however, constitute negligence per se. *Pahanish v. Western Trails, Inc.*, 69 Md. App. 342, 362, 517 A.2d 1122, 1132 (1986). It may be considered evidence of negligence if three conditions are met: (1) the plaintiff is a member of the class of persons the code was designed to protect, (2) the injury suffered is of the type the statute was designed to prevent, and (3) the plaintiff demonstrates that the code violation was the proximate cause of the injury sustained. *Id.*

264. 308 Md. 18, 517 A.2d 336 (1986).

265. *Id.* at 27-32, 517 A.2d at 341-43.

266. *Id.* at 32, 517 A.2d at 343.

267. *Id.* at 32, 517 A.2d at 343-44.

268. 89 Md. App. 217, 597 A.2d 1042 (1991).

269. *Id.* at 223-24, 597 A.2d at 1045.

270. *Id.*

271. *Id.* at 223, 597 A.2d at 1045.

272. *Id.* at 224, 597 A.2d at 1045.

*B. Atlantis and the Liability of Building Contractors Under Maryland Law for Economic Loss*

In the area of construction defects, courts throughout the country have been more willing to extend tort liability to damages for purely economic harm than in the context of product defects. A significant number of states now permit recovery of purely economic losses in negligence actions against architects, developers, designers, and other building contractors.<sup>273</sup> Maryland courts have been slow to address the economic loss doctrine in the construction area. Not until 1986, in the seminal case of *Council of Co-Owners Atlantis Condominium v. Whiting-Turner Contracting Co.*,<sup>274</sup> did the Court of Appeals of Maryland directly confront the issue. In *Atlantis*, a condominium association brought a negligence action against the developer, the general contractor, and the architects of the Atlantis Condominium in Ocean City, alleging that the utility shafts and related electrical work at the condominium were constructed in violation of the building code and the project's plans and specifications.<sup>275</sup> No personal injury or damage to property other than the condominium had occurred, but the defendants' negligence had created a risk of personal injury to the condominium's unit owners.<sup>276</sup> The defendants argued that, in the absence of privity of contract, they owed no tort duty to the unit owners.<sup>277</sup> Alternatively, they argued that they did not owe a duty because the unit owners had suffered only economic loss, not personal injury or property damage.<sup>278</sup>

The court of appeals rejected both of these arguments:

In following the modern trend, we hold that privity is not an absolute prerequisite to the existence of a tort duty. The duty of the architects and the builders in this case, to use due care in the design, inspection and construction of this condominium *extended to those persons foreseeably subject to the risk of personal injury* created, as here, by a latent

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273. For the leading cases permitting recovery of economic loss in negligence against contractors, see *J'Aire Corp. v. Gregory*, 598 P.2d 60 (Cal. 1979); *Barnes v. Mac Brown & Co., Inc.*, 342 N.E.2d 619 (Ind. 1976); *Oates v. Jag, Inc.*, 333 S.E.2d 222 (N.C. 1985); *Quail Hollow East Condominium Ass'n v. Donald J. Scholz Co.*, 268 S.E.2d 12 (N.C. Ct. App. 1980); *Juliano v. Gaston*, 455 A.2d 523 (N.J. Super. Ct. App. Div. 1982); *Kennedy v. Columbia Lumber Mfg. Co.*, 384 S.E.2d 730 (S.C. 1989); *Terlinde v. Neely*, 271 S.E.2d 768 (S.C. 1980); *A.E. Inv. Corp. v. Link Builders, Inc.*, 214 N.W.2d 764 (Wis. 1974).

274. 308 Md. 18, 517 A.2d 336 (1986).

275. *Id.* at 21-22, 517 A.2d at 338-39.

276. *Id.* at 22, 517 A.2d at 338.

277. *Id.* at 23, 517 A.2d at 339.

278. *Id.* at 23-24, 517 A.2d at 339.

and unreasonably dangerous condition resulting from their negligence.<sup>279</sup>

The court concluded that the determination of whether a tort duty should be imposed should depend upon "the risk generated by the negligent conduct, rather than upon the fortuitous circumstance of the nature of the resultant damage."<sup>280</sup> Personal injury or property damage, the court stated, is not a prerequisite to finding such a duty.<sup>281</sup> Where there is merely a risk of death or personal injury, regardless of whether privity exists, a plaintiff may recover the "reasonable cost of correcting the dangerous condition."<sup>282</sup> The court reasoned that a risk of injury will suffice because a home buyer should not have to wait for a personal tragedy to occur in order to recover damages to remedy or repair existing defects.<sup>283</sup>

Thus, the court of appeals in *Atlantis* held for the first time that economic losses—in this case, the costs of remedying code violations and other dangerous conditions in the condominium's construction—were recoverable in a negligence action against parties with whom the plaintiffs enjoyed no privity.<sup>284</sup> This was the first decision in Maryland to make such a holding, either in the context of construction or product defects.

The court of appeals expressly limited its holding in *Atlantis* to instances where the plaintiff is seeking recovery solely for economic damages where a risk of personal injury is also present. The court has not addressed the question of whether risk of property damage would support a tort duty.<sup>285</sup> In *Jacques v. First National Bank of*

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279. *Id.* at 32, 517 A.2d at 343-44 (emphasis added).

280. *Id.* at 35, 517 A.2d at 345.

281. *Id.*

282. *Id.*

283. *Id.* The court of appeals, however, stated that in the absence of actual injury the nature of the risk must be serious. *Id.* at 35 n.5, 517 A.2d at 345 n.5. Conditions which present a risk to general health, welfare, or comfort but fall short of presenting a clear danger of death or personal injury will not suffice. *Id.* Thus, what constitutes "a clear danger of death or personal injury" will vary from case to case.

284. Although the court did not expressly state that economic losses were recoverable in such instances, this is clearly the court's holding. *Id.* at 21, 517 A.2d at 338; see *Boatel Indus., Inc. v. Hester*, 77 Md. App. 284, 307-08, 550 A.2d 389, 401 (1988) (characterizing "risk of death or personal injury" incurred as a result of design and structural defects to plaintiffs' boat as economic loss).

285. In contrast to the *Atlantis* and *Drexel* decisions, courts in other states have not made a distinction on the basis of the nature of the risk generated by a contractor's conduct. For instance, in *Kennedy v. Columbia Lumber & Manufacturing Co.*, 384 S.E.2d 730 (S.C. 1989), the Supreme Court of South Carolina found a legal duty on the part of a builder to refrain from constructing a house that he knows or should know will pose serious risks of *physical* harm, either to persons or property. *Id.* at 737. This duty, according to the court,

Maryland,<sup>286</sup> however, the court set forth, in general terms, when a tort duty for economic loss will be recognized. Although *Jacques* does not involve the liability of a building contractor for economic loss, it clarifies the court's holding in *Atlantis* and is thus important to this discussion.

The plaintiffs in *Jacques*, Mr. and Mrs. Jacques, had entered into a residential sales contract with a third party that was contingent upon their ability to obtain a conventional loan for the balance of the contract price.<sup>287</sup> They submitted an application for a loan to the defendant, First National Bank.<sup>288</sup> An officer of the bank subsequently notified the plaintiffs that the loan they qualified for would not cover the balance of the contract price.<sup>289</sup> When the Jacques requested that the bank deny their application outright, the bank refused.<sup>290</sup> The Jacques proceeded to settlement with the bank's loan after acquiring the balance of the money through personal loans from relatives and a short-term personal loan of \$50,000 from the bank.<sup>291</sup>

The Jacques sued the bank for malicious interference with contract, gross negligence, and negligence.<sup>292</sup> The court of appeals determined that a contract existed between the bank and the Jacques by virtue of statements made by the bank's officer and that this contract included an implied promise to use reasonable care.<sup>293</sup> The issue for the court was whether a concomitant tort duty existed under the circumstances.<sup>294</sup>

The court first reiterated that the mere negligent breach of a contract will not alone sustain an action 'sounding in tort.'<sup>295</sup> In

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was imposed by virtue of the applicable building code, construction industry standards, and public policy. *Id.* (citations omitted). As the court of appeals did in *Atlantis*, the Supreme Court of South Carolina reasoned that a plaintiff need not wait for physical harm to occur before he or she can recover in negligence. *Id.* A builder, the court stated, "is no less blameworthy in such a case where lady luck has smiled upon him and no physical harm has yet occurred." *Id.* The court concluded that a builder may be liable in tort despite the fact that only economic harm was incurred where the builder has (1) violated a building code, (2) deviated from industry standards, or (3) constructed a house that he knows or should know will pose a serious risk of physical harm. *Id.* at 738.

286. 307 Md. 527, 515 A.2d 756 (1986).

287. *Id.* at 528-29, 515 A.2d at 756-57.

288. *Id.* at 529, 515 A.2d at 757.

289. *Id.* at 530, 515 A.2d at 757.

290. *Id.*

291. *Id.*

292. *Id.* at 530-31, 515 A.2d at 757-58.

293. *Id.* at 540, 515 A.2d at 762.

294. *Id.*

295. *Id.* at 534, 515 A.2d at 759 (quoting *Heckrotte v. Riddle*, 224 Md. 591, 595, 168 A.2d 879, 882 (1961)).



determining whether a tort duty should be recognized, the court held that there are two major considerations: “[T]he nature of the harm likely to result from a failure to exercise due care, and the relationship that exists between the parties.”<sup>296</sup> Applying these two factors, the court found that because the nature of the harm involved here was merely economic loss, an “intimate nexus” was required between the parties as a condition to imposing tort liability.<sup>297</sup> This intimate nexus, the court stated, could be satisfied only by contractual privity or its equivalent.<sup>298</sup>

Thus, the court of appeals recognized a sliding scale approach to determining the existence of a tort duty:

We discern from our review of the development of the law of tort duty that an inverse correlation exists between the nature of the risk on one hand, and the relationship of the parties on the other. As the magnitude of the risk increases, the requirement of privity is relaxed—thus justifying the imposition of a duty in favor of a large class of persons where the risk is of death or personal injury. Conversely, as the magnitude of the risk decreases, a closer relationship between the parties must be shown to support a tort duty. Therefore, if the risk created by negligent conduct is no greater than one of economic loss, generally no tort duty will be found absent a showing of privity or its equivalent.<sup>299</sup>

The court held that this intimate nexus requirement had been satisfied.<sup>300</sup> The court reasoned that, in light of the extraordinary financing provisions of the sales contract, the bank had undertaken a significant responsibility when it agreed to process the Jacques’ application and determine the amount for which they qualified.<sup>301</sup> The court also considered the nature of the banking industry as a “public calling,” and noted that “[t]he law generally recognizes a tort duty of due care arising from contractual dealings with professionals such as physicians, attorneys, architects, and public accountants.”<sup>302</sup> The court concluded that a cause of action in negligence exists when a bank “fail[s] to exercise that degree of care which a

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296. *Id.*

297. *Id.*

298. *Id.* at 534-35, 515 A.2d at 759-60. The court further stated that where the risk created is one of personal injury, it is unnecessary to establish a direct relationship, and foreseeability becomes the principle determinant of a tort duty. *Id.* at 535, 515 A.2d at 760.

299. *Id.* at 537, 515 A.2d at 761.

300. *Id.* at 540, 515 A.2d at 762.

301. *Id.* at 540, 515 A.2d at 762-63.

302. *Id.* at 541, 515 A.2d at 763.

reasonably prudent bank would have exercised under the same or similar circumstances."<sup>303</sup>

Thus, the *Jacques* decision clarifies the court's holding in *Atlantis* by more fully describing when a tort duty to avoid economic loss will be recognized under Maryland law, particularly when the resulting harm is other than a risk of personal injury. The determinative factors will be (1) the nature of the harm likely to result from the negligent conduct, without the necessity of actual harm occurring, and (2) the relationship that exists between the parties.<sup>304</sup>

### C. Recovery of Economic Loss Against Contractors Under Other Causes of Action

The court of appeals has also recently discussed the recovery of economic loss in the context of a negligent misrepresentation action, indicating that it will broadly apply the "intimate nexus" test. In *Village of Cross Keys, Inc. v. United States Gypsum Co.*,<sup>305</sup> a condominium's unit owners sued the developer and architect of the project for defective design and construction of the condominium's exterior walls.<sup>306</sup> The developer and architect, in turn, brought a third party negligent misrepresentation action against United States Gypsum, who they alleged had issued a publication containing the specifications for the curtain wall system used in constructing the condominium.<sup>307</sup> The third-party claim contended that United States Gypsum's design in the publication was defective and contained misrepresentations which were relied upon by the architect when designing the condominium's walls.<sup>308</sup>

In determining whether United States Gypsum owed a tort duty to the developer and architect, the court cited the factors established in *Atlantis* and *Jacques*—the relationship between the parties and the nature of the actual or foreseeable harm.<sup>309</sup> The court noted that

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303. *Id.* at 544, 515 A.2d at 764.

304. *Id.* at 534, 515 A.2d at 759. This is provided that the risk involved is of death or personal injury rather than to the general health, welfare or comfort of the plaintiff. *Council of Co-Owners Atlantis Condominium, Inc. v. Whiting-Turner Contracting Co.*, 308 Md. 18, 35 n.5, 517 A.2d 336, 345 n.5 (1986).

305. 315 Md. 741, 556 A.2d 1126 (1989).

306. *Id.* at 745-46, 556 A.2d at 1127-28.

307. *Id.* at 747-49, 556 A.2d at 1128-30. The court did not discuss the liability of the developer and architect to the unit owners. Apparently, the developer settled with the unit owners prior to the appeal. *Id.* at 744 n.2, 556 A.2d at 1127 n.2.

308. *Id.* at 747-49, 556 A.2d at 1128-30.

309. *Id.* at 751-53, 556 A.2d at 1131-32. The court also cited the following factors set forth in *Ashburn v. Anne Arundel County*, 306 Md. 617, 627, 510 A.2d

although *Atlantis* involved negligent conduct, "similar principles apply when negligent misrepresentation is involved."<sup>310</sup> The court assumed that the third-party plaintiffs were seeking recovery for economic loss and considered the evidence of an "intimate nexus" or of "a limitation of the group of those who might be harmed sufficient to avoid the 'specter of unlimited liability, with claims devastating in number and amount crushing the defendant because of momentary lapse from proper care.'"<sup>311</sup> In doing so, the court interpreted the "intimate nexus" requirement very broadly, and found that although United States Gypsum had not sold the design specifications directly to the third-party plaintiffs, there was evidence that it had the "specific intent" that architects and developers in general would adopt those specifications.<sup>312</sup> The court concluded that "it is safe to say [that the defendant] did not develop and publish these detailed drawings, specifications, and technical data tables for some altruistic motive."<sup>313</sup>

The federal district court of Maryland did not consider the existence of an intimate nexus when deciding *Flow Industries, Inc. v. Fields Construction Co.*<sup>314</sup> In *Flow*, a general contractor, Hanks Contracting, sued the manufacturer and distributor of pump motors for allegedly making negligent misrepresentations regarding the delivery date for the pumps.<sup>315</sup> The pumps were not delivered until nearly ten months after the date specified in the purchase order, despite repeated assurances by the distributor that they would soon be delivered.<sup>316</sup> As a result, Hanks Contracting suffered economic losses.<sup>317</sup> Hanks had privity with neither the manufacturer nor the distributor,

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1078, 1083 (1986):

[T]he foreseeability of harm to the plaintiff, the degree of certainty that the plaintiff suffered the injury, the closeness of the connection between the defendant's conduct and the injury suffered, the moral blame attached to the defendant's conduct, the policy of preventing future harm, the extent of the burden to the defendant and consequences to the community of imposing a duty to exercise care with resulting liability for breach, and the availability, cost and prevalence of insurance for the risk involved.

*Village of Cross Keys*, 315 Md. at 752, 556 A.2d at 1131 (quoting *Tarasoff v. Regents of Univ. of Cal.*, 551 P.2d 334, 342 (Cal. 1976)).

310. *Id.* at 754, 556 A.2d at 1132.

311. *Id.* at 757-58, 556 A.2d at 1133-34 (quoting W. PAGE KEETON ET AL., *THE LAW OF TORTS* § 107 (4th ed. 1971)).

312. *Id.* at 758, 556 A.2d at 1134.

313. *Id.*

314. 683 F. Supp. 527 (D. Md. 1988).

315. *Id.* at 529.

316. *Id.*

317. *Id.* The court's opinion does not identify the nature of the economic losses. Presumably, the general contractor incurred lost profits as a result of the delay.

since the pumps were ordered from the distributor by one of Hanks' subcontractors.<sup>318</sup> Applying *Jacques*, the district court found that there was no "special relationship" between the parties that would constitute privity or its equivalent.<sup>319</sup> Indeed, "the parties had deliberately structured their relationships, against the background of well-established construction law and practice, to insulate themselves from one another."<sup>320</sup> The court concluded that "[to] disregard these relationships and to find the substantial equivalence of privity where the parties themselves had intentionally avoided it would be contrary to reason."<sup>321</sup>

## V. CONCLUSION

Under the majority approach, the economic loss doctrine holds manufacturers and building contractors liable to third parties only when some identifiable physical harm has been incurred to either persons or to property other than the product or building structure itself.<sup>322</sup> When the harm is incurred to only the product or structure, courts adopting the economic loss doctrine deny recovery in tort.<sup>323</sup>

This approach is certainly justifiable when the resulting harm is purely pecuniary or qualitative in nature. Contract and warranty law, rather than tort law, provide the appropriate remedy in such instances. The majority approach fails, however, when the resulting

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318. *Id.*

319. *Id.*

320. *Id.*

321. *Id.* Interestingly, with regard to the distributor's negligent misrepresentation claim against the manufacturer, the court took a different approach. Although these parties were in privity, and *Jacques* might suggest that they owed a duty of care to one another, the court stated that *Jacques* was not a negligent misrepresentation case. *Id.* at 529-30. The court of appeals in *Jacques* did not pretend to foretell all of the circumstances under which a tort duty will be imposed upon parties in a direct relationship with each other. Thus, it is too facile to posit the equation that *Martens Chevrolet plus Jacques* automatically equals a tort duty upon those in privity to use reasonable care in what they say to one another.

*Id.* at 530. The court reasoned that to hold that "a contractual relationship itself provides the duty of care necessary for the maintenance of a negligent misrepresentation claim would be to turn the principle into a syllogism. The contract, in effect, would become an 'independent duty imposed by law.'" *Id.* The district court concluded that where "the controversy concerns purely economic losses allegedly caused by statements made during the course of a contractual relationship between businessmen, it is plainly contract law which should provide the rules and principles by which the case is to be governed." *Id.* In effect, the district court in *Flow Industries* turned the "intimate nexus" requirement in *Jacques* on its head.

322. See *supra* note 44.

323. See *supra* note 44.

harm is actual physical damage to the product or structure. Regardless of whether this type of harm occurs in a "sudden and calamitous" manner, the policy reasons in favor of the economic loss doctrine do not support denying liability. Neither contract principles nor warranty law are designed to allow recovery for physical harm to the product itself. Rather, tort law imposes on all persons a standard of reasonable care to avoid causing foreseeable harm to the property or to the person of another. Any distinction between physical damage to the product itself and physical damage to other property is arbitrary. For instance, if a newly purchased boat has plumbing problems that result in water damage to the boat's carpeting, the owner should not be denied recovery in tort merely because no damage has occurred to other property or to the owner himself. Yet, most courts in the country would characterize the damage to the carpeting as an economic loss and deny recovery because no damage to other property or persons was incurred.

Maryland law, in contrast, recognizes that foreseeability should be the principal factor in the determination of whether a tort duty extends to third parties.<sup>324</sup> The nature of the harm resulting from a defendant's negligence is irrelevant.<sup>325</sup> Under *Atlantis* and its progeny, where a mere risk of personal injury results from a contractor's or a manufacturer's negligence, the plaintiff, as well as all others foreseeably subject to this risk, may recover damages, including economic losses. An action will lie for the reasonable cost of correcting the dangerous condition regardless of whether actual harm has yet occurred.<sup>326</sup>

In sum, the significance of *Atlantis* and the recent *Morris* and *A.J. Decoster* decisions cannot be overstated. The Maryland courts have now adopted a consistent approach, applicable in both the construction and products liability contexts, that restores the application of traditional tort standards and dismisses arbitrary distinctions based on the nature of the harm resulting from negligent conduct.

*Michael R. McCann*

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324. Council of Co-Owners Atlantis Condominium, Inc. v. Whiting-Turner Contracting Co., 308 Md. 18, 35, 517 A.2d 336, 345 (1986).

325. *Id.*

326. *Id.*