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LIABILITY OF ARCHITECTS AND ENGINEERS TO THIRD PARTIES: A NEW APPROACH

I. Introduction

The heart of every American metropolis is dominated by the glass and steel of the skyscraper. They epitomize the synthesis of creativity and technical expertise that is the work of architects and engineers. This note considers the effects on that synthesis of the changes that have occurred over the last twenty-five years in the principles that govern the liability of architects and engineers to third parties.

Imagine that somewhere in one of the newest of these buildings a businessman, hurrying to meet a final deadline, enters an elevator carrying the documents for his firm's bid on a multi-million dollar construction project. As the car begins to rise, an accelerometer in the elevator safety system triggers an electronic signal that activates the braking system. The elevator comes to an abrupt halt. Its passenger is stranded for several hours, and the deadline for construction bids passes. Had he not been delayed, the businessman's firm would have undoubtedly won the bid and been guaranteed a three million dollar profit on the project.

The elevator control system had been designed by a brilliant young electrical engineer whose unique application of micro-processing circuitry was a technological breakthrough of wide-ranging consequence. Now the engineer faces the possibility that he will not be able to continue his work if the multi-million dollar negligence suit against him is successful. Even if he is protected by professional insurance, premiums that have already forced him to increase his fees will undoubtedly skyrocket to a point that may jeopardize his practice.

As unlikely as this story may seem, it represents the script of an engineer's nightmare which many in the profession believe possible. Although the legal ramifications are more complicated than the scenario implies, the underlying theme remains valid. That theme is the adverse impact of liability to third parties on the engineering profession.

This note will analyze the legal tests for determining the scope of duty owed by architects and engineers to third parties, not in privity of contract, when they suffer economic loss allegedly caused by the professional's negligent performance of contractual obligations. The note will discuss the inadequacy of both the doctrine of privity of contract and the standard negligence test of foreseeability as a means of defining the scope of architects' and engineers' liability to third parties. As a solution, a test that includes both legal and policy considerations will be advanced. The proposed test serves as a middle ground between greatly restricting liability because of lack of a contractual relationship, as prescribed by the doctrine of privity, and expansively opening architects' and engineers' third party liability by merely requiring that the plaintiff be foreseeable.

The factual circumstances that typically serve as the basis for the cases discussed herein are as follows. An architect or engineer enters into a contract for services and thereby incurs duties and obligations. By some negligent act or

omission the professional breaches his contractual duty, and economic loss to a party not in privity of contract ultimately results. Because the injury results from a breach of contractual duty, courts are unable to look purely to the law of negligence to determine liability. Rather, the courts frequently are concerned with the interaction between contractual duty and tort liability.

Privity of contract is a doctrine which restrictively defines the scope of liability to third parties for breach of contractual duties. The rule simply states that a plaintiff who seeks recovery from a contracting party must also be a party to the contract. Absent privity of contract, no liability exists. Once it is ascertained that the plaintiff did not "sign the contract," further examination of the merits of the suit is precluded, since privity is applied as a matter of law to determine that a cause of action does not exist. Therefore, other considerations such as foreseeability, reliance, and contractual terms are never reached.

Due to the open-and-shut result of the application of the privity doctrine, potential plaintiffs not in privity have frequently included theories of recovery other than negligence in an attempt to prevent being barred from recovery. Therefore, in addition to negligence, theories such as third party beneficiary contract,¹ strict liability,² misrepresentation,³ or warranty⁴ appear in the cases discussed below. Regardless of the theory of recovery, however, this note's focus will remain on the scope of an architect's or engineer's⁵ liability to third parties injured by his negligence.

II. Privity as a Factor in Architects' and Engineers' Liability

Despite variance in theories of recovery, the doctrine of privity provided an effective defense to third party actions against the architect or engineer for negligence.⁶ In fact, it provided such effective protection that it was not until the 1950's that professional liability insurance was considered a necessity.⁷ An architect knew that he could be held liable only to those who directly engaged his services. As a result of the doctrine of privity, the extent of a professional's liability was predictably limited by a contract of employment.

A. Physical Injury Cases

Because of the differences in the nature of the potential injuries, the demise of privity in architects' cases predated the decline of the doctrine in other professions. Although the professional negligence of accountants, lawyers or surveyors almost exclusively results in economic damage, an architect's pro-

1 A.R. Moyer, Inc. v. Graham, 285 So. 2d 397 (Fla. 1973).

2 La Rossa v. Scientific Design Co., 402 F.2d 937 (3d Cir. 1968).

3 Texas Tunneling Co. v. City of Chattanooga, 329 F.2d 402 (6th Cir. 1964).

4 C.W. Regan, Inc. v. Parsons, Brinckerhoff, Quade & Douglas, 411 F.2d 1379 (4th Cir. 1969).

5 Although one case, Rabinowitz v. Hurwitz-Mintz Furniture Company, 19 La. App. 811, 133 S. 498 (1931), did attempt to distinguish between architects and engineers, the legal considerations are identical and will be treated as such here.

6 See, e.g., Geare v. Sturgis, 56 App. D.C. 364, 14 F.2d 256 (1926); Ford v. Sturgis, 56 App. D.C. 361, 14 F.2d 253 (1926).

7 Smay, *A New Look at Professional Liability Insurance*, 28 A.I.A.J. 455 (1957).

fessional negligence can result in both physical injury and economic loss. It was in cases that involved physical injury that third parties first gained a measure of success against architects. The public policy oriented reasoning adopted in the historic New York Court of Appeals decision, *MacPherson v. Buick Motor Co.*,⁸ was applied in these cases. The purposes served by privity, explained the court, were outweighed by the inequity of requiring innocent third parties to bear the burden of physical injuries: "We have put aside the notion that the duty to safeguard life and limb, when the consequences of negligence may be foreseen, grows out of contract and nothing else."⁹ *MacPherson* thus represents a more sophisticated approach to determining liability to third parties, because the court considers not only the contractual relationship but also policy considerations.

*Paxton v. Alameda County*¹⁰ was an early case in which a California appellate court implicitly abandoned the privity requirement. *Paxton* involved an appeal by an architect from a judgment against him for negligent preparation of plans. Evidence at trial revealed that the architect had agreed to design and supervise a construction project and that during the course of the work the plaintiff, a construction worker, fell through the roof of the structure and sustained serious injuries. He alleged that the architect had been negligent in the design of the roof. On appeal, the court held that the evidence at trial did not support a negligence verdict. The court reached its decision without a discussion of privity, which suggests that recovery might have been available had there been sufficient proof. The panel also implied that an action for negligent supervision could have been sustained by the facts.

The New York Court of Appeals case of *Inman v. Binghamton Housing Authority*¹¹ is frequently cited as the leading case in this field.¹² In *Inman*, although the court affirmed the dismissal of a negligence action against the defendant architect, it enunciated the abandonment of privity implicit in *Paxton*. In this case, the architect designed an apartment building for a co-defendant, a local housing authority. The plaintiff was a tenant's child who was injured in a fall from a stoop. It was alleged that the architect had negligently failed to provide a railing in the plans. The court specifically adopted the criteria used in *MacPherson* to eliminate the privity requirement. Subsequent analysis of the evidence, however, revealed that the certain peril to life and limb required by *MacPherson* was not present. Later cases involving physical injury are almost

8 217 N.Y. 382, 111 N.E. 1050 (1916). In *MacPherson*, the plaintiff was injured when a wheel of an automobile manufactured by the defendant collapsed and the plaintiff was thrown from the car. Since the plaintiff had purchased the automobile from a retail dealer, no privity of contract existed between the plaintiff and the manufacturer. The court held, however, that where a product, if negligently made, is reasonably certain to place life and limb in danger, and the manufacturer of the product knows that it will be used by persons other than the purchaser, the manufacturer is under a duty of care to those users to make the product carefully. The court rejected the semantic distinctions between inherently dangerous things and imminently dangerous things that had been relied on in previous cases. The duty to protect human life and limb was held broader than the scope of contractual undertakings.

9 *Id.* at 390, 111 N.E. at 1053.

10 119 Cal. App. 2d 393, 259 P.2d 934 (1953).

11 3 N.Y.2d 137, 164 N.Y.S.2d 699, 143 N.E.2d 895 (1957).

12 Andrew, *Surety Recovery from the Architect or Engineer—why not?* 8 FORUM 571 (1973). ACRET, ARCHITECTS AND ENGINEERS: THEIR PROFESSIONAL LIABILITY § 10.4 at 167 (1977).

unanimous in their extension of duty to third parties without regard to privity.¹³

B. Economic Injury Cases

When the injury suffered is economic there is, at least in the view of some commentators,¹⁴ a question concerning the availability of a cause of action. Examination of cases that involve purely economic loss reveals that privity is well on its way to extinction. A minority of states still retain the doctrine, but the trend indicates that there will be continued attrition among the ranks.

A 1932 case from the Eighth Circuit Court of Appeals, *Hall v. Union Indemnity*,¹⁵ dispensed with the requirement of privity where an architect had certified a payment to a contractor in violation of his contractual obligation to withhold payment pending satisfactory completion of work. This case, however, proved an exception to the then prevailing rule of privity.¹⁶ It was not until twenty years later that abandonment of privity in cases involving economic loss gained widespread acceptance.

*State v. Malvaney*¹⁷ was another case of improper authorization of payment. The Mississippi Supreme Court upheld a judgement for the plaintiff surety in a negligence action against the defendant architect. The architect had released a final payment to a contractor who left the project before it was completed. The surety who bonded the contractor was called in to complete the work left undone. The plaintiff fulfilled its obligations and then sued the architect to recover the amount of the loss. The court held that lack of privity did not prevent recovery.

In addition to surety companies,¹⁸ other classes of plaintiffs have been successful in third party actions against architects and engineers. In *M. Miller Co. v. Central Contra Costa Sanitary District*,¹⁹ a California appellate court reversed a summary judgement in favor of the defendant engineer in a negligence action brought by a construction contractor. In formulating a bid on a sewer system the contractor relied on a soil report made to the engineer's client, the sanitary district, by the defendant engineer. The report negligently failed to disclose certain soil instabilities which resulted in the contractor's expenditure of almost one million dollars more than the amount bid. The trial court granted a summary judgement to the engineer because of the lack of contractual relation

13 See, e.g., *Montijo v. Swift*, 219 Cal. App. 2d 351, 33 Cal. Rptr. 133 (1963); *Miller v. De Witt*, 37 Ill. 2d 273, 226 N.E. 2d 630 (1967). *Laukkanen v. Jewel Tea Co.*, 78 Ill. App. 2d 153, 222 N.E.2d 584 (1966); *Simon v. Omaha Public Power Dist.*, 189 Neb. 183, 202 N.W.2d 157 (1972).

14 ACRET, *supra* note 12, at 169; SWEET, LEGAL ASPECTS OF ARCHITECTURE & ENGINEERING AND THE CONSTRUCTION PROCESS § 34.03 at 741 (1970).

15 61 F.2d 85 (8th Cir. 1932).

16 In *Hall* the architect was not a party to the action. The owner sued a contractor's surety for the cost of completing a construction project after cost overruns occurred. The architect's negligence was imputed to the owner because the architect acted as the agent of the owner. This contributory negligence defeated the claim against the surety. The abandonment of privity may have been attributable to the lack of direct attack on the architect.

17 221 Miss. 190, 72 So. 2d 424 (1954).

18 See, e.g., *Aetna Insurance Co. v. Hellmuth, Obata & Kassabaum, Inc.*, 392 F.2d 472 (8th Cir. 1968); *Peerless Insurance Co. v. Cerny & Associates, Inc.*, 199 F.Supp. 951 (D.C. Minn. 1961); *United States v. Rogers & Rogers*, 161 F. Supp. 132 (S.D. Cal. 1958); *Calandro Development, Inc. v. R.N. Butler Contractors, Inc.*, 249 So. 2d 254 (La. Ct. App. 1971); *Westerhold v. Carrol*, 419 S.W.2d 73 (Mo. 1967).

19 198 Cal. App. 2d 305, 18 Cal.Rptr. 13 (1961).

between the parties, but the appellate court reversed on the ground that privity was not a prerequisite for recovery.

A.E. Investment Corp. v. Link Builders, Inc.,²⁰ a Wisconsin Supreme Court case, was an appeal from the overruling of an architect's demurrer to a negligence action brought by the tenant of a building whose construction the architect supervised. It was alleged that the architect negligently failed to determine the composition of the subsoil and that as a result the building settled. Damage to the walls and floors made the premises untenable, and the plaintiff was required to expend a considerable amount of money to relocate. The court affirmed the overruling of the demurrer and stated that the lack of privity did not eliminate the possibility that a duty is owed to a third party where economic loss results.

The list of states that have abandoned privity when economic loss is involved is long²¹ but not all inclusive. The clearest case to the contrary is the Indiana appellate court case of *Peyronnin Construction Co. v. Weiss*,²² which affirmed the trial court's sustaining of a demurrer based on lack of privity between the parties. In *Peyronnin*, a subcontractor had relied on the calculations of the defendant engineer in submitting a bid for excavation work. The calculations were erroneous, and the subcontractor was unable to complete the work for the bid price. The prime contractor had to hire another subcontractor to complete the excavation and then sued the engineer to recover the losses incurred. The court said that the cause of action could not be maintained without an allegation of a contractual relationship between the parties. As is characteristic of opinions that uphold the doctrine, there was no discussion of the underlying reasons for retaining the privity requirement.

In a case factually similar to *Peyronnin*, another court refused to allow a cause of action against an engineer for cost overruns that resulted from erroneous excavation estimates. *Delta Construction Co. of Jackson v. City of Jackson*,²³ a Mississippi Supreme Court case, held that the form of the action, contract or tort, is immaterial in determining the applicability of privity:

Whenever a wrong results from the breach of a contract merely, an action or redress, whether in form *ex contractu* or *ex delicto*, can be maintained only by a party to the contract . . . [T]he demurrers were properly sustained because the suit in tort for the alleged negligence of the Engineers is charged to have arisen under terms of contract under which there was no privity of contract between the Engineers and the Contractor.²⁴

20 62 Wis. 2d 479, 214 N.W.2d 764 (1974).

21 See *E.C. Ernst, Inc. v. Manhattan Constr. Co. of Texas*, 551 F.2d 1026 (5th Cir. 1977); *Detweiler Bros., Inc. v. John Graham & Co.*, 412 F. Supp. 416 (E.D. Wash. 1976); *Cooper v. Jevne*, 56 Cal. App. 3d 860, 128 Cal. Rptr. 724 (1976); *A.R. Moyer, Inc. v. Graham*, 285 So. 2d 397 (Fla. 1973); *Craig v. Everett M. Brooks*, 351 Mass. 497, 222 N.E.2d 752 (1967).

22 137 Ind. App. 417, 208 N.E.2d 489 (1965).

23 198 So. 2d 592 (Miss. 1967).

24 *Id.* at 597. This case appears to conflict with *State v. Malvaney*, 221 Miss. 190, 72 So. 2d 724 (1954). See text accompanying note 17 *supra*. The conflict was explained in *Engle Acoustic & Tile, Inc. v. Grenfell*, 223 So. 2d 613 (Miss. 1969), where *Malvaney* was distinguished on the ground that state law required a surety bond in that case. Where a purely private contract is involved, on the other hand, privity of contract is still required.

Several other states²⁵ still retain privity in architects' and engineers' cases that involve economic loss. It is quite possible, however, that a direct confrontation would result in a repudiation of the doctrine in some of them.²⁶ In still others, exceptions and limitations to the rule make its viability questionable.²⁷ The overall trend underscores the limited applicability of the doctrine in architects' and engineers' professional liability cases.

III. The Privity Rationale

Whether accountants, lawyers or engineers were involved, privity was the traditional rule which governed liability to third parties. Absent privity of contract, an injured third party could not recover damages caused by the negligent acts or omissions of the professional. The professional owed no duty of care to third parties not in privity. The accepted method of determining the existence of a duty was an inquiry into the foreseeability of harm to the plaintiff.²⁸ The doctrine of privity prevented the extension of liability to the full limits of foreseeability. The widespread acceptance of privity indicated that there existed valid reasons for a rule that conflicted with an established principle of law.

The principal reason for the doctrine is explained in the famous New York Court of Appeals decision of *Ultramares Corporation v. Touche*.²⁹ The facts in *Ultramares* are familiar. The defendant accountant was sued by a plaintiff lending institution for negligent misrepresentation. The lender had extended credit to the accountant's client based on the accountant's certification of financial stability. Justice Cardozo refused to allow a third party to recover for negligent misrepresentation on the basis of lack of privity. The reason cited for upholding the privity doctrine was that it afforded the defendant protection from unlimited liability: "If liability for negligence exists, a thoughtless slip or blunder . . . may expose accountants to a liability in an indeterminate amount for an indeterminate time to an indeterminate class."³⁰

25 See *Blecick v. School District No. 18 of Cochise County*, 2 Ariz. App. 115, 406 P.2d 750 (1965); *Barnes v. Hampton*, 198 Neb. 151, 252 N.W. 2d 138 (1977); *Roban Construction v. Hazleton Housing Auth.*, 67 Pa. D. & C.2d 130 (C.P. 1974).

26 For example, *Texas Tunneling Co. v. City of Chattanooga*, 329 F.2d 402 (6th Cir. 1964) held that Tennessee law did not allow a subcontractor to maintain a cause of action against an engineer without privity of contract. The engineer had failed to include test drilling data in information provided to the city, which had requested bids on the construction of a tunnel. The subcontractor relied on the engineer's information in the preparation of its bid and incurred losses because of the negligent omission. It is doubtful that the same result would occur today in light of subsequent developments. *Ford Motor Co. v. Lonan*, 217 Tenn. 400, 398 S.W.2d 240 (1966), a products liability case, allowed recovery for economic losses despite a lack of privity. Also, a case relied on in *Texas Tunneling*, *Howell v. Betts*, 211 Tenn. 134, 362 S.W.2d 924 (1962), has been limited by *Tatera v. Palumbo*, 224 Tenn. 262, 453 S.W.2d 780 (1970), such that *Howell* would no longer control.

27 See *Hunt v. Star Photo Finishing Company*, 115 Ga. App. 1, 153 S.E.2d 602 (1967); *Lumber Products v. Hiriart*, 255 So. 2d 783 (La. Ct. App. 1971); *Engle Acoustic & Tile, Inc. v. Grenfell*, 223 So. 2d 613 (Miss. 1969); *Hamill v. Foster-Lipkins Corporation*, 41 App. Div. 2d 361, 342 N.Y.S.2d 539 (1973).

28 "[T]he orbit of the danger as disclosed to the eye of reasonable vigilance would be the orbit of the duty." *Palsgraf v. Long Island R. Co.*, 248 N.Y. 339, 162 N.E. 99, 100 (1928).

29 255 N.Y. 170, 174 N.E. 441 (1931).

30 *Id.* at 179, 174 N.E. at 444.

Cardozo's analysis distinguished the concepts of foreseeability and unlimited liability. He reasoned that even though the accountant may have foreseen reliance on its certificate by third party lenders, more was required to impose liability on the defendant: "Foresight of these possibilities may charge with liability for fraud. The conclusion does not follow that it will charge with liability for negligence."³¹ The purpose of the doctrine of privity is to remove the burden of unlimited liability from the defendant.

Beyond this limitation on indeterminate liability, it is difficult to formulate with certainty any other reasons behind the doctrine of privity. The handful of judicial opinions that continue to rely on it are curiously lacking in any discussion of its merits. Somewhat ironically, the best guide to ascertain what courts consider additional rationale for the doctrine can most often be found in opinions that abandon the doctrine. Most cases that involve architects and engineers focus on the potential for unlimited liability. It is impossible, however, to reconcile this reason with the decisions that approve of the doctrine of privity.

As an example consider *Peyronnin Construction Co. v. Weiss*,³² in which an Indiana appellate court held that a contractor could not recover from an engineer absent privity of contract. The opinion of the court lacked any discussion of the reasons for requiring privity. The facts of the case reveal that the unlimited liability criteria would dictate rejection of the doctrine. At the time the defendant engineer prepared calculations for the excavation, he knew that they were to be used in the preparation of bids. Any underestimate would surely result in financial loss to the contractor who successfully bid on the project. Additionally it was known that only a single party could win the bid, which limited the potential plaintiffs to one. The only unknown factor was the identity of the prospective plaintiff. Since the facts of this case had already limited the defendant's liability to a single, foreseeable plaintiff, the protective benefits afforded by the privity doctrine were not necessary. Therefore, its application was unwarranted if the sole purpose of privity is to prevent unlimited liability. Where the reason for the law ceases to exist, blind application based on tradition is unacceptable.

The longevity of the doctrine indicates that there are additional reasons for its application. One of these was touched tangentially in *Ultramares*: the loss of a contracting party's control over contractual duties.³³ Privity protects against an extension of the duties embodied in a contract to encompass third parties to whom no duty was intended. This rationale is akin to that of third party beneficiary contracts, and in many cases the action is brought under that theory. Even where the intent of the contract has not been held sufficient to maintain the third party beneficiary action, tort actions have been maintainable.³⁴

The issue here is actually one of fairness: whether a party who has not paid for the professional's expertise should have the privilege of relying on it. This concern was shown in one of the examples used in *Ultramares* to illustrate the

31 *Id.* at 183, 174 N.E. at 446.

32 137 Ind. App. 417, 208 N.E.2d 489 (1965).

33 "The assumption of one relation will mean the involuntary assumption of a series of new relations, inescapably hooked together . . . The law does not spread its protection so far . . ." *Ultramares Corp. v. Touche*, 255 N.Y. 170, 174 N.E. 441, 448 (1931).

34 *Detweiler Bros., Inc. v. John Graham & Co.*, 412 F. Supp. 416 (E.D. Wash. 1976); *A.R. Moyer, Inc. v. Graham*, 285 So. 2d 397 (Fla. 1973).

effects of expanding the defendants' potential liability:

Title companies insuring titles to a tract of land, with knowledge that at an approaching auction the fact that they have insured will be stated to the bidders will become liable to purchasers who may wish the benefit of a policy without payment of a premium.³⁵

Whereas complete limitation of contractual obligations may be contrary to public policy,³⁶ courts generally consider it desirable³⁶ to honor the intentions of the parties.³⁷

Another purpose of privity, and perhaps the strongest force that must be considered, is a policy to limit the professional's liability. This does not mean that courts bestow gratuitous favoritism on professionals at the expense of other litigants. Rather, courts recognize that the benefits conferred on society by the professional may dictate that professional liability be somewhat restricted. Although rarely expressed in judicial opinions,³⁸ it seems to be a policy inherent in the cases that uphold privity. The practical effect of the doctrine is to confer virtual immunity on the architect or engineer from third party suit.³⁹

To summarize, the most commonly applied rationale for the doctrine of privity is the prevention of unlimited liability. Before the question of foreseeability is reached, the scope of the potential liability must be considered in determining whether a duty of care to a third party exists. A second reason for the doctrine is the prevention of the unfair reliance on professional services without payment of any consideration. Third, privity allows the court to limit the professional's liability in recognition of the importance of his services to the public.⁴⁰

IV. Replacement of Privity

The antithesis of the privity doctrine is the construct of a universal duty.⁴¹ Not all courts have gone so far as to impose such a duty. Most courts rely on the

35 255 N.Y. at 188, 174 N.E. at 448.

36 For example, UCC § 2-719(3) makes an exclusion of damages for personal injury *prima facie* unconscionable.

37 There is a countervailing aspect to the fairness issue. In projects supervised by an architect or engineer, the construction contract may give the professional wide-ranging powers over the contractors. Some courts have imposed a duty because of this degree of control. "The power of the architects to stop the work alone is tantamount to a power of economic life or death over the contractors. It is only just that such authority, exercised in a relationship, carry legal responsibility." *United States v. Rogers & Rogers*, 161 F. Supp. 132, 136 (S.D. Cal. 1958).

38 In *Broyles v. Brown Engineering Co.*, 275 Ala. 35, 151 So. 2d 767 (1963), where a plaintiff alleged breach of warranty against a civil engineer, the court discussed implied warranties with respect to professionals. It concluded that there are valid reasons for treating professionals differently from other defendants.

39 Witherspoon, *Architect's and Engineer's Tort Liability*, 16 DEF. L.J. 408, 410 (1967).

40 Another reason is cited in *Westerhold v. Carrol*, 419 S.W.2d 73 (Mo. 1967). It was said that privity protected the ability of contracting parties to alter the terms of their contract. The *Westerhold* court properly dismissed this reason as unimportant because the existence of a duty to a third party does not usually prevent the contracting parties from changing their agreement.

41 "The proposition is this: Every one owes to the world at large the duty of refraining from those acts that may unreasonably threaten the safety of others." *Palsgraf v. Long Island R. Co.*, 248 N.Y. 339, 162 N.E. 99, 103 (1938) (Andrews, J., dissenting).

general principle of negligence to determine whether a duty is owed to a third party. In architects' and engineers' cases involving physical injury, the guiding principles of products liability are applied.⁴² Where economic losses result, the legal concepts of foreseeability and unlimited liability are most often used to determine the existence of a duty.⁴³ This test avoids the inflexibility of privity while retaining its primary purpose, the prevention of indeterminate liability. This approach, however, does not take into account the other purposes of the doctrine, limitation of contractual duties and protection of the professional. An implication that might be drawn is that these purposes are no longer considered important under modern legal thinking.

The inadequacy of the foreseeability/unlimited liability approach, however, was recognized by the California Supreme Court. That court indicated that there are public policy arguments for restricting the scope of the duty owed by a professional to third parties. In *Biakanja v. Irving*,⁴⁴ the court dealt with a notary public⁴⁵ who drew up a will for a client. The notary failed to have the will properly witnessed, and when the testator died, the will was denied probate. As a result, the testator's sister received a smaller portion of the estate by intestate succession than she would have received under the will. She therefore brought a negligence action against the notary to recover her loss. The court held that lack of privity did not absolutely bar third party recovery, but rather that public policy factors had to be considered in determining the availability of a remedy. The factors cited were: 1) the extent to which the transaction was intended to affect the plaintiff; 2) the foreseeability of harm to the plaintiff; 3) the degree of certainty that the injury was suffered; 4) the connection between the conduct and the injury; 5) the moral blame; and 6) the policy of preventing future harm. The court applied these tests and held that a cause of action against the notary existed.

The *Biakanja* test has been followed in a number of cases,⁴⁶ including several that involve architects and engineers.⁴⁷ The test does not, however, appear to be the final solution in cases involving economic loss.

The *Biakanja* test embodies some elements that are not public policy considerations, but that instead are elements of any negligence case; namely, the certainty of the harm and the proximity of causation. Subsequent cases have added to the list of factors that require consideration. *Kornitz v. Earling & Hiller, Inc.*⁴⁸ is a Wisconsin case brought by a purchaser of an apartment house

42 *Inman v. Binghamton Housing Authority*, 3 N.Y.2d 137, 164 N.Y.S.2d 699, 143 N.E.2d 895 (1957).

43 *A.R. Moyer, Inc. v. Graham*, 285 So. 2d 397 (Fla. 1973); *Craig v. Everett M. Brooks Co.*, 351 Mass. 497, 222 N.E.2d 752 (1967). See also *Rusch Factors v. Levin*, 284 F. Supp. 85 (D.R.I. 1968); *Rozny v. Marnul*, 43 Ill. 2d 54, 250 N.E.2d 656 (1969).

44 49 Cal. 2d 647, 320 P.2d 16 (1958).

45 Although the defendant in *Biakanja* was not an attorney, it is clear that the result in the case would not have been different had he been an attorney.

46 See, e.g., *Tarasoff v. Regents of Univ. of California*, 17 Cal. 3d 425, 131 Cal. Rptr. 14, 551 P.2d 334 (1976) (psychiatrist); *Lucas v. Hamm*, 56 Cal. 2d 583, 15 Cal. Rptr. 821, 364 P.2d 685 (1961) (attorney); *Licata v. Spector*, 26 Conn. Sup. 378, 225 A.2d 28 (C.P. 1966) (attorney).

47 See e.g., *Rogers & Rogers*, 161 F. Supp. 132 (S.D. Cal. 1958); *Cooper v. Jevne*, 56 Cal. App. 3d 860, 128 Cal. Rptr. 724 (1976); *Westerhold v. Carrol*, 419 S.W.2d 73 (Mo. 1967).

48 49 Wis. 2d 97, 181 N.W.2d 403 (1970).

against a mortgage lender on a theory of false representations and negligence. The defendant mortgagee had negligently approved final payment to the builder of the apartment complex without first assuring that all claims for labor and materials had been paid. The plaintiff purchased the apartment house from the owner developer after the defendant had represented that all construction bills had been paid. When outstanding bills were presented to the plaintiff, he brought suit against the mortgagee. In affirming the overruling of a demurrer, the Supreme Court of Wisconsin said that the existence of a cause of action depended on public policy factors and not on the existence of privity. One such factor noted by the court was the impact on the mortgage lending industry. Because of the lack of a factual basis in the record, the reviewing court declined to make the policy decision and suggested that the trial court hear evidence on the policy issues.

The Wisconsin Supreme Court reiterated its belief that public policy factors may preclude liability in *A. E. Investment Corp. v. Link Builders, Inc.*⁴⁹ The case was an appeal from a lower court's overruling of a defendant architect's demurrer pleading lack of privity. The court's ruling was narrowly limited to a finding that privity of contract was not a prerequisite for recovery from an architect for economic loss. The plaintiff was a tenant of a building designed by the defendant architect. When the foundation settled the premises became untenable and caused a loss of profits for which the plaintiff sought recovery. The court held that lack of privity did not bar recovery. In dictum, however, the court added that public policy factors may be considered in determining whether a third party can recover damages for economic losses. The court did not make a policy decision because the record from the court below did not include sufficient information. The court did cite several cases⁵⁰ that discussed a common policy factor: the burden that would be placed on the party liable.

An excellent discussion of the *Biakanja* test appears in the majority and dissenting opinions of *Connor v. Great Western Savings and Loan Assn.*⁵¹ In this case the California Supreme Court went beyond the *Biakanja* test to consider other factors. In *Connor* an action was brought by purchasers of homes in a new real estate development. The defendants were parties involved in the project, including Great Western Savings and Loan Assn., who had provided financing for the construction of the homes. It was alleged that the buildings were of substandard construction and that the defendant loan company had been negligent in approving the financing. The court applied the *Biakanja* test to reverse the trial court's dismissal of the action. Significantly, the court extended the scope of its analysis to include such factors as the increase in home construction costs, industry-wide insurance, and the impact on small construction companies.

V. Policy Considerations in Limiting Liability of Architects and Engineers to Third Parties

From the cases discussed above, it is clear that courts are concerned about

49 62 Wis. 2d 479, 214 N.W.2d 764 (1974).

50 *Hass v. Chicago & North Western Ry. Co.*, 48 Wis. 2d 321, 179 N.W.2d 885 (1970); *Colla v. Mandella*, 1 Wis. 2d 594, 85 N.W.2d 345 (1957).

51 69 Cal. 2d 850, 73 Cal. Rptr. 369, 447 P. 2d 609 (1968).

the potential detrimental effects on professionals if third party liability is extended. In attempting to formulate a comprehensive test to apply to architects and engineers, it is appropriate to consider in some detail how liability to third parties affects the profession.

A review of professional publications reveals the concern about unlimited liability within the profession, as illustrated by articles with such telling titles as *The Great Sue Massacre*⁵² and [Scape] *Goat Hunting; A New National Pastime*.⁵³ In a less alarmist vein, publications such as *Professional Engineer* and *Architectural Record* regularly include articles that concern the legal aspects of professional practice. A lawyer need only mention his trade in the presence of an engineer to generate a heated discussion of the adverse impact that the law has had on his profession.

The most obvious impact is on professional liability insurance rates.⁵⁴ Although the situation has not yet reached the crisis proportions present in the medical malpractice field, the current rate spiral gives cause for concern. A reduction in liability to third parties would not reverse the tide of rising costs but would reduce the specter of inflated recoveries. It is the fear of those recoveries which forces the small practitioner to obtain coverage far in excess of what might be considered reasonable. The increased cost of this coverage is especially burdensome to the young architect and, as a result, the trend towards larger firms has been accelerated. The result has been a decrease in the creative potential of the individual practitioner.⁵⁵

The first reply of those who favor no limitations on liability is that the professional merely has to pass on his increased insurance costs to those who use his services. A similar argument was advanced to support the demise of privity in accountant's liability. There it was reasoned that the accounting firms were in a better position to absorb the loss than were innocent plaintiffs.⁵⁶ The accountants could spread the burden among all those who used their services, whereas the plaintiff investor would have to bear the entire loss himself. The same argument is not as convincing, however, when applied to architects or engineers.

A survey of the cases shows that the most frequent plaintiffs in actions for economic loss are contractors, subcontractors and surety companies. Each of these parties has entered into a business arrangement and accepted some accompanying risk. The parties are of roughly equal bargaining power and have similar economic leverage. It is not unreasonable to require contractors and other third parties to bear the burden of self-protection. If they plan to rely on the professional services of an engineer, they should be required to hire their own

52 *Why Mining Machinery Costs More: The Great Sue Massacre*, 82 COAL AGE 106 (May 1977).

53 Segraves, *Goat Hunting; A New National Pastime*, 7 CHEM. TECH. 139 (Mar. 1977).

54 In 1975, premiums for architects, which had tripled over the previous four years, increased between 75% and 105%. Although third party liability claims are just under 25% of all claims paid, on the average they are larger and more widely publicized than claims made by the architect's clients. Cauty & Dunlop, *Of Liability, Litigation and Insurance*, 64 A.I.A.J. 17 (Jul. 1975); Griffin, *Expanding Liability*, 2 ARCH. PLUS 62 (Jul.-Aug. 1974).

55 *Sweet*, LEGAL ASPECTS OF ARCHITECTURE & ENGINEERING AND THE CONSTRUCTION PROCESS § 34.01 at 739 (1970).

56 *Rusch Factors, Inc. v. Levin*, 284 F. Supp. 85, 91 (D.R.I. 1968).

consultant. This consultant would not duplicate the work of the original architect but instead would review the work in light of his client's particular needs. This requirement does not affect the final distribution of costs, since both the architect and the contractor are able to pass the expenses on to the purchaser of the final product. The advantage gained by limiting third party liability in this manner is a reduction in the number of large and usually well-publicized recoveries against architects. As discussed previously, this reduces the pressure to obtain excessive amounts of insurance protection or to seek refuge in large firms.

Emphasis on the status of the parties would not mean a denial of all third party recovery. In the hypothetical situation presented at the beginning of this article, it would hardly be reasonable to require every user of an elevator to do so at his own risk. The plaintiff was in no position to protect himself from the loss; therefore, this would be a factor that would tend to dictate liability. Also, by taking into consideration the relative status of the parties, some of the appearance of unfairness currently perceived by the profession would be eliminated.⁵⁷

The most important effect of widespread liability to third parties, and yet the hardest to document, is the chilling effect on creativity. The architect who strikes out into a new form or the engineer who pioneers a new technology is particularly vulnerable. Where most architects would not dare venture, the creative practitioner thrives. This makes him a prime candidate for a malpractice action when his creation is a financial disaster because his work is not that of the more traditional architect. It is here that the law may have its most subtle yet most egregious effect.

The availability of third party liability coupled with the publicity of a few disproportionate recoveries serves to deter creativity.⁵⁸ One professional engineer views the subject as follows:

On one hand, the lure of expanded services, which in extreme cases may be necessary for the architect's survival, pulls him toward those new professional services. On the other hand, the warnings of insurers anxiously assessing new hazards in an already perilous field, push him back into the safer, more comfortable rut of traditional architectural services.⁵⁹

The "expanded services" referred to were joint ventures which would combine the resources of architects, engineers and other professionals to accomplish projects beyond the capabilities of even the largest firms. Some of these ventures were held uninsurable because of the potential liability for economic losses.⁶⁰

⁵⁷ This unfairness was discussed in Rosenberg, *Contingency Fees*, 104 *FOUNDRY M. & T.* 32 (Jun. 1976). The article involves an industry in which the engineer's liability usually takes the form of a products liability action; the discussion, however, is apropos to professional negligence in general. The author was critical of the continued expansion of third party recovery where the third party was an industrial customer. The advent of strict liability was seen as a means to protect the social welfare but not the interests of industry. The need to protect business interests is far less demanding than the need to protect innocent third parties. The article called for a statutory modification of products liability law to recognize this difference.

⁵⁸ The articles cited in note 53 *supra*, point out that third party recoveries are usually larger and receive substantially more publicity than contractual recoveries.

⁵⁹ Griffin, *Expanding Liability*, 2 *ARCH. PLUS* 62 (Jul.-Aug. 1974).

⁶⁰ *Id.* at 62.

Expanding liability has affected creativity on both ends of the spectrum by forcing the single practitioner into larger associations and by limiting the horizons of high-powered associations.

Obviously the solution does not lie in a return to the doctrine of privity. Its inflexibility prevents any consideration of the merits of a case. The most promising course of action is to adopt the principles of *Biakanja v. Irving*,⁶¹ with a modification of the factors that the court should consider. The existence of a duty of due care should be based on the following legal and policy factors:

- 1) the extent to which the transaction was intended to benefit the plaintiff,
- 2) the foreseeability of harm to the plaintiff,
- 3) the potential for unlimited liability,
- 4) the effect of liability on the profession,
- 5) the relative burden of prevention and the ability to bear the loss,
- 6) the moral blame, and
- 7) the policy of preventing future harm.

The weight and interaction of these seven factors must be determined on a case-by-case basis.

The existence of a duty of due care should be determined by the judge as a matter of law. Judicial opinions will tend to fill out the structure previously outlined. If weighing of the factors were left to a jury, few conclusions could be drawn from the verdict. The judge may be able to make his decision based on the pleadings and affidavits submitted in support of a motion for summary judgment. Where no duty can be established, the litigants will be saved the time and expense of a trial. This is particularly important to the professional, who depends heavily on his reputation. A trial on the merits is costly, in terms of both money and prestige, even when the verdict is favorable. Another unique aspect of architects' and engineers' liability cases is the extent of involvement of the professional in the preparation of the case. The technical considerations involved frequently necessitate an abnormally large amount of client-attorney contact. Early resolution of cases by summary judgement obviates the necessity of trying unworthy claims. Where the factors considered by the court weigh in favor of the plaintiff, a trial on the merits will be necessary.

VI. Conclusion

The special protection against third party liability afforded architects and engineers by the requirement of privity of contract has undergone steady erosion during the last twenty-five years. The concept has been reduced to an historical footnote in all but a few jurisdictions, and even those jurisdictions limit its application to cases that involve economic loss. Both the stated and unstated purposes of the doctrine are insufficient to outweigh the inflexibility of the rule. The formalistic nature of the privity doctrine is incompatible with the modern trend towards wider access to the courts for adjudication on the merits of a claim.

With the exception of foreseeability, however, the complete removal of

61 See text accompanying note 43 *supra*.

limitations on third party recovery against architects and engineers has had adverse effects on the profession. In recognition of this fact, some courts have discussed policy factors that may dictate a sort of limitation on the availability of a cause of action brought by a third party against a professional. An analysis of the impact of third party liability on architects and engineers suggests a list of factors that should be considered in determining whether a cause of action exists. The judge should consider:

- 1) the extent to which the transaction was intended to benefit the plaintiff,
- 2) the foreseeability of harm to the plaintiff,
- 3) the potential for unlimited liability,
- 4) the effect of liability on the profession,
- 5) the relative burden of prevention and the ability to bear the loss,
- 6) the moral blame, and
- 7) the policy of preventing future harm.

Based on these factors the judge would determine as a matter of law whether an action by a third party were cognizable.

The result is that third party liability of architects and engineers would be determined on the basis of realistic considerations of law and policy. No longer would liability to third parties turn on the mere existence or non-existence of a contractual relation between the parties, as prescribed by the formal doctrine of privity. At the same time, liability would be based on more factors than foreseeability alone. Liability of architects and engineers thus becomes a much more flexible concept determined by equitably balancing various factors relevant to the protection and expectations of all litigants. Such a prescribed solution is not only reasonable to administer by the courts, it is also immeasurably more sensitive to the parties involved.

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