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On the Differences Between Blood and Red Ink: A Second Look at the Policy Arguments for the Abrogation of the Economic Loss Rule in Consumer Litigation

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Edward T. O'Donnell, David I. Weiss, and Daniel L. Kaplan

Abstract

The long-running debate concerning the scope of the economic loss rule¹ presents issues which are important in themselves and as illustrations of broader questions.² Litigants and commentators champion the opposing schools of thought through close analysis of precedent;³ the exchange of views as to the nature of tort law and contract law;⁴ and occasionally, economic analysis.

KEYWORDS: red link, blood, litigation

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TABLE OF CONTENTS

| | | |
|-------|--|-----|
| I. | INTRODUCTION | 924 |
| II. | THE AGENDA | 926 |
| III. | AN OUTLINE OF LANDMARK CASES AND THE CLASSICAL ARGUMENTS FOR THE OPPOSING POSITION | 927 |
| IV. | HARDER QUESTIONS FOR THE DEFENSE AND SOME ANSWERS | 932 |
| | A. <i>The Lure of Oversimplification</i> | 933 |
| | B. <i>Wolves in Sheep's Clothing</i> | 935 |
| V. | THE LACK OF A SINGLE, COMPELLING OBJECTIVE | 936 |
| VI. | SOME COSTS OF REFORM | 938 |
| | A. <i>The Uncertainties in the New Body of Law</i> | 938 |
| | B. <i>The Burden at the Working Level</i> | 940 |
| VII. | THE UNCERTAINTY AS TO WHO WOULD GAIN, HOW, AND WHY | 942 |
| | A. <i>The Purchaser Without Tears</i> | 942 |
| VIII. | THE FALSE PROMISE OF EXCEPTIONS AND DISTINCTIONS | 944 |
| | A. <i>Assumed Boundaries and Their Life Expectancy</i> | 944 |
| IX. | SOME DRAWBACKS TO THE "CATASTROPHIC RISK" AND "SEPARATE PRODUCT" EXCEPTIONS | 945 |
| X. | WHO IS THE HAND AND WHO IS THE EYE? | 953 |
| XI. | THE POSSIBILITY OF LESS DISRUPTIVE ALTERNATIVES | 954 |
| XII. | GOALS OR ANALYSIS | 956 |

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| | | |
|-------|--|-----|
| A. | <i>Compensation</i> | 956 |
| B. | <i>Deterrence—Goal or Mirage?</i> | 958 |
| C. | <i>Higher Prices—The Skull Behind the Mask</i> | 959 |
| D. | <i>Insurance and the Sharing of Pain</i> | 959 |
| XIII. | CONCLUSION | 964 |

I. INTRODUCTION

The long-running debate concerning the scope of the economic loss rule¹ presents issues which are important in themselves and as illustrations

1. The significance of the economic loss rule is that a buyer seeking recovery for the loss caused by product failure must plead the cause in warranty or contract. In most jurisdictions, the buyer cannot recover if the event did not cause personal injury or damage to property other than the product itself. A recent decision of the Florida Supreme Court is representative. The plaintiff alleged flaws in concrete caused the walls and ceilings of a condominium to crack, and ultimately pieces fell, narrowly missing residents; however, there were no actual injuries. *Casa Clara Condominium Assoc., Inc. v. Charley Toppino & Sons, Inc.*, 620 So. 2d 1244 (Fla. 1993). The economic loss rule prohibited recovery because the product did not cause personal injury or damage to anything other than itself. *Id.* at 1246 (citing *East River S.S. Corp. v. Transamerica Delaval, Inc.*, 476 U.S. 858 (1986)); *Danforth v. Acorn Structures, Inc.*, 608 A.2d 1194 (Del. 1992) (treating sovereign error as exception to economic loss rule); *AFM Corp. v. Southern Bell Tel. & Tel. Co.*, 515 So. 2d 180 (Fla. 1987); *Florida Power & Light Co. v. Westinghouse Elec. Corp.*, 510 So. 2d 899 (Fla. 1987); *cf. Sunnyslope Grading, Inc. v. Miller, Bradford & Risberg, Inc.*, 437 N.W.2d 213, 217-18 (Wis. 1989); *Spychalla Farms, Inc. v. Hopkins Agric. Chem. Co.*, 444 N.W.2d 743, 747 (Wis. Ct. App. 1989). Note, it is sometimes suggested that a better term would be “commercial loss.” See the opinion of Judge Posner in *Miller v. United States Steel Corp.*:

The Millers are attempting to use tort law to recover the cost of replacing a defective product sold to them for use in their business. This cost is called in law an “economic loss,” to distinguish it from an injury to the plaintiff’s person or property (property other than the product itself), the type of injury on which a products liability suit usually is founded. It would be better to call it a “commercial loss,” not only because personal injuries and especially property losses are economic losses, too—they destroy values which can be and are monetized—but also, and more important, because tort law is a superfluous and inapt tool for resolving purely commercial disputes. We have a body of law designed for such disputes. It is called contract law. Products liability law has evolved into a specialized branch of tort law for use in cases in which a defective product caused, not the usual commercial loss, but a personal injury to a consumer or bystander.

Miller, 902 F.2d 573, 574 (7th Cir. 1990).

of broader questions.² Litigants and commentators champion the opposing schools of thought through close analysis of precedent;³ the exchange of views as to the nature of tort law and contract law;⁴ and occasionally, economic analysis.⁵ Their heartfelt arguments reflect origins in the distinct, self-sufficient assumptions and insights characteristic of commercial and product liability law. Perhaps, as a result, neither side answers the others' contentions directly.⁶

Those who favor abolishing the rule use an account of a buyer's predicament as prelude. Once the stage is set, there follows an assertion that an otherwise dispositive point of law—a statute of limitations, or perhaps precedent as to the enforceability of waiver—should not apply to the particular case. Ultimately, references to the humanitarian purposes of

2. See *Neibarger v. Universal Coops., Inc.*, 486 N.W.2d 612 (Mich. 1992); Jay M. Zitter, Annotation, *Strict Products Liability: Recovery for Damage to Product Alone*, 72 A.L.R.4TH 12 (1989).

3. See Steven G.M. Stein et al., *A Blueprint for the Duties and Liabilities of Design Professionals After Moorman*, 60 CHI.-KENT L. REV. 163 (1984) (discussing a painstaking effort to reconcile the law of professional malpractice with distinctions between contract and tort law established by Illinois case law).

4. Some courts and scholars are concerned the possible expansion of the tort system would distort the laboriously worked out balances of the U.C.C. See Sarah B. Parker, Note, *Economic Loss in Product Liability: Strict Liability or the Uniform Commercial Code*, 28 B.C. L. REV. 383 (1987) (suggesting rough categorization of those who would create a limitation to economic loss rule on the basis of the type of plaintiff and those who would do so on the basis of type of injury). A University of Pennsylvania article supports the general definition of economic loss which plaintiffs' advocates offer. See Comment, *Manufacturers' Liability to Remote Purchasers for "Economic Loss" Damages—Tort or Contract?*, 114 U. PA. L. REV. 539 (1966). However, the author concludes on a broader issue: "[T]he tort rationale of risk distribution and the doctrine of assumption of risk, while appropriate in personal injury cases, seem wholly inappropriate when the injury is only the loss of the value of the purchaser's bargain." *Id.* at 549. The article goes on to say it would be ironic "if the tort doctrine which was evolved to rescue the personal injury area from the 'intricacies of the law of sales' were to imprison the economic loss area with inapposite tort concepts." *Id.*; see also *State ex rel. W. Seed Prod. Corp. v. Campbell*, 442 P.2d 215, 217-18 (Or. 1968), *cert. denied*, 393 U.S. 1093 (1969); Robert L. Rabin, *Tort Recovery/Negligently Inflicted Economic Loss*, 37 STAN. L. REV. 1513 (1985).

5. William K. Jones, *Product Defects Causing Commercial Loss: The Ascendancy of Contract Over Tort*, 44 U. MIAMI L. REV. 731 (1990).

6. The reason for that failure of communication may be a belief on the part of plaintiffs' lawyers that the term of art, strict liability, embodies social realities so deep they are beyond debate. Conversely, the defense lawyers' instinct is that once an issue is labeled as one of "products liability" and "policy," the battle is lost.

modern product law arrive at a conclusion that contract law has given way to tort law and that the individual rule or precedent is no longer pertinent. However, on closer examination, lawyers have not demonstrated a link between premise and conclusion. Moreover, the attorney has not shown that contract law is inadequate in theory, or that the commercial system is unfair in its practical workings.

Those who defend the rule operate on a different intellectual dimension than their adversaries. Typically, the defense does not challenge their adversaries' assumptions that a change in the rule would advance the goals of product liability. Rather they finesse, by praising contract doctrines as the natural channel for business⁷ to provide the parties with an opportunity to negotiate an arrangement to satisfy the needs of each.

This article tries to narrow the gap by recasting the case for the economic loss rule in terms of the general concepts of products liability and practical litigation.

II. THE AGENDA

Taking the classic "contract" defense of the economic loss rule as a starting point, we attempt a more utilitarian and literal minded approach. Our objective is to meet the concerns which lead others to call for change head on. In the course of that effort, we urge the courts to prohibit strict liability claims for pure economic injury, even when the potential plaintiff is not a commercial entity. The economic loss rule, contract law, and the commercial system have functioned sufficient enough to let people buy and sell goods for hundreds of years. The working arrangements of everyday life should not change because of a shift in fashion among tort and contract theories.

7.

If the ultimate user were allowed to sue the manufacturer in negligence merely because an article with latent defects turned out to be bad when used in "regular service" without any accident occurring . . . manufacturers would be subject to indiscriminate lawsuits by persons having no contractual relations with them, persons who could thereby escape the limitations, if any, agreed upon in their contract of purchase. Damages for inferior quality, per se, should better be left to suits between vendors and purchasers since they depend on the terms of the bargain between them.

Trans World Airlines, Inc. v. Curtiss-Wright Corp., 148 N.Y.S.2d 284, 290 (1955).

Each suggestion rests on the following observations and contentions:

1) Those who criticize the rule should identify its specific problems and explain why existing law cannot meet their needs. Often, statutory reforms or traditional common law rulings, tailored to a specific need, would solve the problem with minimum side effects. In contrast, a sweeping pronouncement that tort law rather than contract law is to govern an undefined group of cases will saddle the lower courts with practical, doctrinal, and even constitutional problems.

2) A shift to tort liability will force manufacturing corporations to take steps in self-protection. The ideal would be for those steps to improve safety and to achieve other goals of product liability; however, there are reasons to expect different results.

3) Trigger phrases such as "compensation," are important and valid for their purpose—the identification of the goals of product liability. However, they are neither specific nor objective enough to answer questions at the heart of this debate. Plaintiffs' advocates propose a new system which depends upon a vast increase in the number of tort lawsuits for "economic loss." The court would be unable to determine whether that approach would be as efficient as the existing system or whether it would work at all.

4) The analysis of legal issues in terms of social needs and practical impact is legitimate. But judges should decide whether a particular social need exists rather than treat that central question as a background assumption settled long ago in the academic literature. To the extent the argument for reform takes on that routinized character, strict liability will expand through momentum and stylishness rather than the reasoned analysis of new circumstances.

III. AN OUTLINE OF LANDMARK CASES AND THE CLASSICAL ARGUMENTS FOR THE OPPOSING POSITION

At an early stage in the development of modern product law, the Supreme Court of New Jersey held that the purchaser could sue in strict liability for the value lost when a new rug developed a line which would not "walk out."⁸ The broader teachings of *Santor v. A & M Karagheusian*⁹ emphasizes that the economic burden of injuries from products should be

8. *Santor v. A & M Karagheusian, Inc.*, 207 A.2d 305 (N.J. 1965).

9. *Id.*

distributed throughout the system¹⁰ and that the law should make it easier for the consumer-plaintiff to recover.¹¹

The California Supreme Court led the counterattack in *Seely v. White Motor Co.*¹² If any jurist grasped both the significance and limitations of the new concepts, it was the authors of the opinions in *Greenman v. Yuba Power Products, Inc.*¹³ and *Escola v. Coca Cola Bottling Co.*¹⁴ Nevertheless, Justice Traynor refused to apply strict liability to a claim for the failure of a truck to operate properly.¹⁵ Instead, he focused on the difference between the risk to physical safety and the possibility that a product will not meet the economic expectations of the buyer.¹⁶ The former danger, he wrote, is the logical province of the law of torts; the latter, the traditional subject matter of contract and the law merchant.¹⁷

Two decades later, in *East River Steamship Corp. v. Transamerica Delaval, Inc.*,¹⁸ the United States Supreme Court held there was no tort claim where a turbine failed, impairing the ship's performance, but not damaging the vessel itself or any other product. Specifically, Justice Blackmun reasoned that: 1) a claim of that nature is best understood in terms of warranty since the product did not meet the consumer's expecta-

10. The court was explicit on that point:

[W]hen the manufacturer presents his goods to the public for sale he accompanies them with the representation that they are safe for the intended use. . . . The obligation of the manufacturer thus becomes what in justice it ought to be—an enterprise liability, and one which should not depend upon the intricacies of the law of sales.

Id. at 311-12; see Patricia A. Brown & Jay M. Feinman, *Economic Loss, Commercial Practices, and Legal Process: Spring Motors Distributors v. Ford Motor Company*, 22 Rutgers L.J. 301 (1991) (emphasizing different concepts of rational analysis).

11.

The purpose of such liability is to insure that the cost of injuries or damage, either to the goods sold or to other property, resulting from defective products, is borne by the makers of the products who put them in the channels of trade, rather than by the injured or damaged person who ordinarily are [sic] powerless to protect themselves.

Santor, 207 A.2d at 312; see also Parker, *supra* note 4, at 393 (discussing cases which followed *Santor*).

12. 403 P.2d 145 (Cal. 1965).

13. 377 P.2d 897 (Cal. 1963).

14. 150 P.2d 436 (Cal. 1944).

15. *Seely*, 403 P.2d at 149.

16. *Id.*

17. Note that the Traynor opinion includes a thoughtful consideration of policy questions; many of the authors' suggestions are elaborations on those themes. See *id.* at 145.

18. 476 U.S. 858 (1986).

tions; 2) contract law is well suited to such commercial disputes because it enables the parties to define their own agreement and their respective obligations; and 3) warranty law has built-in boundaries and restraints, whereas tort law may subject the defendant to limitless damages.¹⁹

19. *Id.* at 871-74. *East River* has often been referred to as the "majority rule" in products liability cases involving the economic loss issue. The Supreme Court of Alabama adopted the *East River* rule in *Lloyd Wood Coal Co. v. Clark Equipment Co.*, 543 So. 2d 671 (Ala. 1989), in which the court denied recovery to the lessee of a front-end loader that caught fire and damaged itself. The court stated the "tort concern with safety is reduced when an injury is only to the product itself" unlike the situation in which a "person is injured, the 'cost of an injury and the loss of time or health may be an overwhelming misfortune.'" *Id.* at 673 (quoting *Escola*, 150 P.2d at 441 (Traynor, J., concurring)). The opinion urged that consequential economic loss caused by the failure of the product is more easily and readily insurable; that the parties should be free to allocate risks among themselves; and finally, that warranty law contains an adequate remedy with necessary limitations on liability, that is, privity and remoteness. *Id.* at 673-74. In his dissent, Justice Jones urged that the majority view leaves the plaintiffs "remediless" when they do not suffer personal injury or damage to the property (other than to the product itself). *Id.* at 674 (Jones, J., dissenting). In his view, "to be relegated to commercial law (breach of warranty) for their remedy is to be *without* a remedy." *Id.* (Jones, J., dissenting). Indeed, Justice Jones suggested that "[t]he manufacturer of standardized products either elects to warrant the product or not warrant the product, it can limit both the quality and the quantity of that warranty as it sees fit." *Lloyd*, 543 So. 2d at 675 (Jones, J., dissenting). In contrast, he "never heard of the purchaser of a piece of machinery having any input into either the nature or the extent of any warranty given by the manufacture." *Id.* (Jones, J., dissenting).

Justice Jones urged that:

The law should make no distinction between classes of plaintiffs whose injury or loss results from a defective product . . . [and there] is no valid policy reason for denying a cause of action in tort to those plaintiffs who, fortuitously, have not suffered personal injury or property damage other than damage to the defective product itself, but who . . . are denied an action in contract because the defective product is not covered by any form of extended warranty.

Id. (Jones, J., dissenting). This result should be compared to the Alabama Supreme Court's opinion in *Dairyland Insurance Co. v. General Motors Corp.*, 549 So. 2d 44 (Ala. 1989), in which the court reversed the trial court's decision granting the defendant's summary judgment on a negligence theory of liability. In *Dairyland*, a van caught fire while the plaintiff was driving it. Although the plaintiff was not injured, the van was totally destroyed. In reversing the negligence count, the Alabama Supreme Court held that the plaintiff set forth a "scintilla of evidence" to satisfy the Alabama proof standard to show a defect in the van. *Id.* at 46. The court applied *Lloyd* to bar the plaintiff's claims of negligent manufacture and extended manufacturer liability, yet distinguished the decision from the plaintiff's negligent repair theory wherein the plaintiff claimed he reported a problem with the van's lights to the dealer's service personnel and staff did not follow normal procedures in response to such a claim. *Id.*

The Superior Court of Pennsylvania also adopted *East River* in *Rem Coal Co. v. Clark Equipment Co.*, 563 A.2d 128 (Pa. Super. Ct. 1989), in which the plaintiff company

The New Jersey court returned to the issue in *Spring Motors Distributors v. Ford Motor Co.*²⁰ The plaintiff, Spring Motors, was a corporation in the business of selling and leasing trucks. Spring Motors purchased a

purchased a front-end loader from the defendant company to use in a strip mining business. The plaintiff company sued the seller on a strict liability theory after the loader caught fire and was severely damaged. The Pennsylvania Superior Court held that contract law defined the appropriate limits of recovery, regardless of the nature of the risk created by the malfunction. *Id.* at 133.

Three years later, in *Jones v. General Motors*, 631 A.2d 665 (Pa. Super. Ct. 1992), the Pennsylvania Superior Court extended its holding in *Rem Coal* to cover situations in which the plaintiff is an ordinary consumer, rather than a commercial enterprise. The plaintiff purchased a new Chevrolet pick-up truck, which caught fire and was destroyed while parked and empty. The court affirmed the trial court's summary judgment for the defense. *Id.* at 665. The Third Circuit decision, *Pennsylvania Glass Sand Corp. v. Caterpillar Tractor Co.*, 652 F.2d 1165 (3d Cir. 1981), referred to *Rem Coal* when the product defect alleged was the lack of a fire suppression system on a front-end loader. The damage to the loader occurred as a result of a sudden and calamitous fire. The Third Circuit qualified the defect as dangerous, and held the plaintiff did have a tort cause of action for the event. *Id.* at 1174. This conclusion was premised on the federal appellate court's prediction that the Pennsylvania Supreme Court, if confronted with the issue, would adopt an intermediary position between *Seely* and *Santor*. *Id.* A conclusion which would ban recovery for economic losses in general, but allow for tort recovery when the product posed a risk of injury to the person or other property of the plaintiff. *Id.* at 1168. In application, however, the Third Circuit held the plaintiff failed to state a cause of action in tort because it only alleged a non-dangerous defect and a gradual deterioration of the product, and neither involved a calamitous event. *Id.* at 1174-75.

Ultimately, *East River* led the Third Circuit to reconsider. In *Aloe Coal Co. v. Clark Equipment Co.*, 816 F.2d 110 (3d Cir.), *cert. denied*, 484 U.S. 853 (1987), the purchaser of a front-end loader sued the manufacturer in breach of warranty, strict liability, and negligence when the vehicle unexpectedly caught fire and suffered damage. No other property was damaged, nor did any personal injury result from the incident. After reviewing *East River*, the Third Circuit concluded the Supreme Court's analysis was so persuasive that it would be followed by the Pennsylvania courts. *Id.* at 117. The court retreated from the intermediary position it established in *Pennsylvania Glass*, and adopted the "bright-line" test enunciated in *East River*. *Id.* In application, *East River* mandated the Third Circuit deny recovery in tort, despite the calamitous nature of the event and the potentially dangerous nature of the defect. *Id.* at 117. Similarly, in *King v. Hilton-Davis*, 855 F.2d 1047 (3d Cir. 1988), *cert. denied*, 488 U.S. 1030 (1989), potato farmers sued in tort alleging the seed potatoes they purchased were treated with Fusarex, a chemical manufactured by Hilton-Davis. The Third Circuit reversed the jury verdict in favor of the plaintiffs. *Id.* at 1048. Referring to *East River* as the majority rule, the Third Circuit determined that the distinctive issue of the economic loss rule was whether the product "injures only itself." *Id.* at 1050. The court concluded that the allegedly contaminated seed potatoes did not constitute "other property," hence, it was an instance involving only economic loss. *Id.* at 1051.

20. 489 A.2d 660 (N.J. 1985).

shipment of thirty Fords, opting for the transmissions the Clark Equipment Company supplied, rather than standard Ford equipment. When Ford and Clark Equipment were unable to eliminate malfunctions in the transmissions, the dealer had to sell the trucks at a loss. A little more than four years after the purchase, Spring Motors filed suit against Ford and Clark Equipment for breach of warranty, strict liability, and negligence. The trial court dismissed the complaint on the ground that all claims were barred by the U.C.C.'s four year statute of limitations. On appeal, the appellate division held that the six year statute of limitations for tort actions applied rather than the shorter warranty limit. After surveying New Jersey opinions on strict liability, the intermediate appellate court concluded the extension of strict liability to economic loss would be consistent with that development.²¹

The defendants did not cross-appeal. Accordingly, the issue before the New Jersey Supreme Court was whether a commercial buyer of defective goods is limited to U.C.C. remedies and is prevented from asserting claims in strict liability and negligence.²²

In the majority opinion, Justice Pollock did not retreat from the *Santor* rule insofar as a future case might involve a consumer purchaser.²³ The court held, nevertheless, that the U.C.C. governed the sale of a fleet of trucks to Spring Motors, a large dealership, and its reasoning left no doubt that the result should be the same in any litigation arising from a transaction between commercial parties which results in purely economic loss.²⁴ In his

21. *Id.* at 663.

22. *Id.* at 662.

23. The majority opinion in *Spring Motors* concluded the lack of privity would not have barred the warranty action. *See id.* The concurring opinion expresses concern regarding the effect the majority's reasoning in a case which did not arise from such a clearly commercial relationship. *Id.* at 677 (Handler, J., concurring). Each is consistent with an argument that the result should be the opposite in a pure "consumer" case.

24. Justice Pollock observed the U.C.C. "constitutes a comprehensive system for determining the rights and duties of buyers and sellers with respect to contracts for the sale of goods." *Spring Motors*, 489 A.2d at 665. He emphasized strict liability traditionally applied to product defects which cause physical injury, but in this case there was a lack of privity between the consumer and the manufacturer of the defective product. *Id.* at 674. The U.C.C. is designed to simplify disputes between business entities. *Id.* On that basis, the court concluded commercial parties which suffer economic losses because of defective goods are limited to their rights and remedies under the U.C.C., and may not resort to tort theories such as strict liability and negligence. *Id.*

The majority opinion further stated that the delineation of the boundary between strict liability and the U.C.C. requires appreciation not only of the policy considerations underscoring both sets of principles, but also of the role of the legislature as a coordinate branch of government. *Id.* By enacting the U.C.C., Congress adopted a carefully conceived

concurring opinion, Justice Handler approved the result in this instance, specifically because the parties maintained a long-standing commercial relationship, and it would be natural to expect the U.C.C. to govern. Nevertheless, he expressed concern that there would not always be such a clear-cut distinction between a commercial buyer and a "consumer," and that there will be instances of unequal bargaining power,²⁵ even though each participant is a commercial entity.

Our brief synopses would do an injustice if they suggested the courts ignored the policy dimension of the issue.²⁶ Yet even in the landmark decisions, the common ground fades into generalization and stylized abstraction. Those seeking to change the rule speak of steps to equalize bargaining power, but investigate neither the extent of the disparity of bargaining power nor the effects of the change. Those who would support the rule show a sturdy faith in bargaining, but say little of the numerous instances in which there was no bargaining and never could have been.

IV. HARDER QUESTIONS FOR THE DEFENSE AND SOME ANSWERS

The classic defense of the economic loss rule draws intellectual force from a faith that individuals and corporations know their own needs and that bargaining between them is an efficient method for the allocation of risks

system of rights and remedies to govern commercial transactions. *Spring Motors*, 489 A.2d at 674. Allowing *Spring Motors* to recover from Ford under tort principles would dislocate major provisions of the U.C.C. *Id.* For example, application of tort principles would obviate the statutory requirement that a buyer give notice of a breach of warranty, and would deprive the seller of the ability to exclude or limit its liability. In sum, the U.C.C. represents a comprehensive statutory scheme satisfying the needs of the world of commerce, and courts should pause before developing judicial doctrines that might dislocate the legislative structure.

25. The examples Justice Handler used included sales of such vehicles to:

a travelling salesperson or a small-scale trucker, or a carpenter, plumber, electrician, or landscape gardener. It does not follow automatically that if the vehicle proves to be defective, the U.C.C. shall apply as the exclusive remedy to govern recovery of direct or consequential economic loss solely because such purchaser is in business or bought the vehicle for use in business. Rather, the analysis should turn on whether a purchase made in that kind of setting, even if for a business or commercial purpose, is sufficiently distinguishable from a purchase for personal use by an ordinary private consumer to justify a difference in remedial treatment.

Id. at 679. Justice Handler went on to discuss the possibility that the remote buyer might not be able to benefit by the abolition of vertical privity if he did not receive notice of the manufacturer's disclaimer of liability. *Id.* at 680-81.

26. *Spring Motors*, in particular, represents a direct and conscientious evaluation of policy considerations. *See id.* at 671.

and burdens.²⁷ Plaintiffs respond, however, that the reasoning grows hollow when a corporation is pitted against one who does not have the sophistication or even the opportunity to negotiate.²⁸

At the least, the critics of the rule are correct that the purchaser gets no opportunity to bargain with the intermediate sellers, even those who played vital roles in the process that led to the complete product.²⁹ The answer, for the most part, must be that which the Supreme Court suggested in *East River*: harshness in some individual cases is the price for a stable commercial system.

Finding the defense of the majority view not completely satisfactory ourselves, we take consolation in exploring the countervailing unrealities of some arguments against the rule.

A. *The Lure of Oversimplification*

In *Santor*, Justice Francis indicated that the manufacturer's responsibility should be the same whether the damage is to a person or to a rug—one injury is like another if each is the consequence of a defect in a product.³⁰ The assertion was epigrammatic and forceful. But symmetry in doctrine bumps against reality. Personal injury and economic losses are not the same thing in ordinary speech, in practical effect, or in legal analysis.³¹ The

27. For example, in *Spring Motors* the court held when the action is between "commercial parties with comparable bargaining power," neither strict products liability nor negligence may be used as a basis for recovering "benefit of the bargain" or consequential loss damages. *Spring Motors*, 489 A.2d at 670-71. The disappointed commercial entity will be left to its remedies, if any, under the U.C.C. *Id.* at 674; *see also* *Scandinavian Airlines Sys. v. United Aircraft Corp.*, 601 F.2d 425, 429 (9th Cir. 1979).

28. For a recent case following the majority position on the economic loss rule, but distinguishing it on policy grounds, see *Detroit Bd. of Educ. v. Celotex*, 493 N.W.2d 513 (Mich. Ct. App. 1992), in which the parties did not have an opportunity to negotiate because even though the defect in the product existed from the outset, it was unknown. *Celotex* held that asbestos is unique in the law, and determined the risk was not the type to be allocated to the parties to the negotiation process. *Id.* at 518-19.

29. *Casa Clara*, 620 So. 2d at 1248 (Barkett, J., dissenting). There are a number of cases which take opposing stands as to whether the economic loss rule applies when the parties are not in privity. *See* *Twin Disc, Inc. v. Big Bud Tractor*, 772 F.2d 1329, 1333 (7th Cir. 1985); *Hap's Aerial Enter. v. General Aviation Corp.*, 496 N.W.2d 680, 681-82 (Wis. Ct. App. 1992). These cases raise the point that the rule is appropriate only when there is a commercial relationship.

30. *Santor*, 207 A.2d at 309.

31. *But see* *Rabin*, *supra* note 4, at 1513-15 (arguing the opposing view).

distinctions between them are in fact central to modern products liability doctrine.

One difference lies in the demands each makes on the trial courts. Commercial cases involve numerous parties in a variety of relationships. Personal injury cases are often fearfully complex for other reasons. Nonetheless, they present more concentrated and manageable fact issues in the sense that the injury victims generally suffer harm of a single type. In the more significant of these cases such as design litigation, a decision for—or against—one claimant on the liability issue would require the same conclusion as to the others.³²

More important holdings, such as *Greenman*, arose from the human experience that the economic consequences of major personal injuries tend to devastate the individual in a way that others do not.³³

32. A commentator suggests the reason why recovery is permitted for personal injury is:

[I]n personal injury situations such as the airplane crash and building collapse, the injury victims constitute a single class—they suffer a type of harm in common. Barring recovery for any individual victim would mean barring the recovery for all victims. Putting aside the accountants' liability cases, incidents involving widespread economic loss are quite different from the cases of multiple personal injury. The chain of commercial losses triggered by the accidental closure of a plant or death of a person are "ripple effect" losses; in an important sense they implicate a secondary group of victims who suffer highly diverse types of harm.

Rabin, *supra* note 4, at 1533.

33. *Greenman*, 377 P.2d at 897. The response might be that there are many economic catastrophes which are also devastating to human victims, but that question is beyond the scope of this paper. For better or for worse, the view that personal injury damages are unique seems established.

Other differences between economic loss and personal injury involve the fact that economic loss is easily quantified in advance, and thus is easily insurable. *See Lloyd*, 543 So. 2d at 673 (holding defendant was not strictly liable for having sold front-end loader that caught fire and damaged itself). Damages which may be quantified in advance of the transaction are most efficiently handled as part of the bargain, rather than by time-consuming and expensive litigation after the fact.

Even in the case of defective automobiles—the classic situation enabling tort recovery for buyers—courts draw a clear distinction between economic losses and personal injuries. For example, in *Hiigel v. General Motors Corp.*, 544 P.2d 983, 989 (Colo. 1975), the court refused to invoke strict liability to cover lost profits resulting from a defect in a truck purchased for business use.

Lost profit is clearly more "economic" than other types of loss which have formed the basis for strict liability claims. However, the rationale distinguishing lost profit claims from personal injury claims applies equally as well to other claims for economic loss damages. *See, e.g., Prairie Prod., Inc. v. Agchem Div. Pennwalt Corp.*, 514 N.E.2d 1299 (Ind. Ct. App.

B. *Wolves in Sheep's Clothing*

Another observation is equally impressionistic, yet it has both a pedigree and a moral. Critics urge that the doctrine protects sellers at the expense of “consumers”—a value-charged phrase. But a closer look at an opinion which expresses that concern often reveals that it is a business, rather than a “hapless consumer” which pushes to change the economic loss rule.³⁴

In *Seely*, for instance, Justice Traynor observed that the complaint of overreaching by the seller had little force because the plaintiff itself was a corporation.³⁵ The working hypothesis drawn is that companies often struggle to cut back the rule and that they act rationally when they do so. The benefits of the change would flow to them as much as to individuals. Corporations, after all, are buyers as often as sellers. Equally important, they have the resources and institutional attention span to take full advantage of the change. An argument that the rule protects corporations against individuals requires a closer and more skeptical scrutiny.

The buyer who is not a corporation is not necessarily so poor or unsophisticated as the sacred texts of products liability suggest. In *Casa Clara*, for example, one of the individual claimants bought his own land and hired a general contractor and architect.³⁶ Rather being a contract of

1987) (denying recovery of lost profits to farmer who purchased pesticide that failed to eliminate corn earworms, thus, deferring to legislative framework set forth in U.C.C.); *Brown v. Western Farmers Ass'n*, 521 P.2d 537 (Or. 1974) (rejecting lost profit as basis for recovery when farmer was unable to sell chickens that ate defective feed supplied by defendant); *Star Furniture Co. v. Pulaski Furniture Co.*, 297 S.E.2d 854 (W. Va. 1982) (refusing to extend strict liability recovery of lost profits for plaintiff who purchased defective clock). *But see* *Jones v. Bender Welding & Mach. Works*, 581 F.2d 1331 (9th Cir. 1978) (allowing recovery of lost profits under maritime negligence law by fishermen who purchased defective boats); *Cooley v. Big Horn Harvestore Sys., Inc.*, 767 P.2d 740 (Colo. Ct. App. 1988), *aff'd in part, rev'd in part*, 813 P.2d 763 (1991) (allowing recovery on negligence theory to dairy farmers who lost profits because grain storage system failed to prevent spoilage); *Chubb Group Ins. Cos. v. C.F. Murphy & Assocs.*, 656 S.W.2d 766 (Mo. Ct. App. 1983) (holding plaintiff entertainment companies could recover lost profits from collapse of arena built by defendants).

34. *See, e.g.*, *Mead Corp. v. Allendale Mutual Ins. Co.*, 465 F. Supp. 355 (N.D. Ohio 1979) (holding in favor of large corporation that successfully relied on precedent emphasizing the plight of individual); *American Drugstores v. AT&T Technologies*, 583 N.E.2d 694 (Ill. 2d App. Ct. 1991) (refusing to extend strict liability when several businesses sued telephone company after fire at switching station disrupted telephone service in community because no one sustained any injury or property damage).

35. *Seely*, 403 P.2d at 151-52.

36. *Casa Clara*, 620 So. 2d at 1249.

adhesion, the agreement gave him the right to attorneys' fees in the event of the seller's breach.³⁷

Even a more representative individual buyer need not be a victim *per se*. The argument against the rule frequently includes the assertion that an ordinary person is overwhelmed by contracts and fine print. Yet people cope with contracts every day; the generality is overbroad and even patronizing. True, some transactions are difficult. The purchase of a home, for example, is the largest investment the ordinary person ever makes.³⁸ Everyone knows that, and as a result, buying a house is the occasion in a lifetime when the ordinary person is most likely to hire a lawyer to represent his or her interests.³⁹ The lawyer, moreover, can do that work at an acceptable cost; this is customary in nature and the issues are well settled. If the courts open the way to novel tort-based claims, that predictability would diminish. What would this change bring the public in return?

V. THE LACK OF A SINGLE, COMPELLING OBJECTIVE

Although the debate is one of the great pieces of products liability lore, it still is unclear what the advocates of change strive to accomplish.⁴⁰ One answer, implicit in the complaints of unequal bargaining power, is they think the change would make the process of negotiation and compromise more equitable.

Even if given the chance, would the ordinary consumer dicker with dozens of suppliers over the prices and specifications of engine blocks, seat springs, shatterproof glass, and hundreds of other individual components rather than buy a complete automobile?⁴¹ To the extent the buyer would not do such a thing, the case for dismantling the commercial system to cure the supposed lack of opportunity grows more dubious.

Any initial impression of unfairness fades even more when one considers the buyer has enforceable rights against the seller of a house or of

37. *Id.*

38. *Id.* at 1247 (citing *Conklin v. Hurley*, 428 So. 2d 654 (Fla. 1983)).

39. *Id.*

40. In the individual case, of course, the change could lead to a plaintiff's victory, but that is not a coherent intellectual basis for broad change.

41. In theory, if the buyer had an opportunity to bargain, the buyer could demand a written extension of warranty from the supplier of each component. The common sense response is that the possibility of product failure of one of the components sometime in the future is not enough to justify all the paperwork. However, the same possibility could not justify adding new complexities to lawsuits and imposing new burdens on the courts.

any other product.⁴² Further, the seller almost always was the buyer of components at a preceding stage.⁴³ To survive, it had to remember that its own customer might complain and even sue if any component should fail. This put pressure on the business to search for good materials and to bargain for warranty coverage, for the consumer's ultimate benefit.⁴⁴ This indirect

42. *See, e.g.,* Hartley v. Ballou, 209 S.E.2d 776 (N.C. 1974) (extending implied warranty recovery against builder of house that flooded during rainy weather); George v. Veach, 313 S.E.2d 920 (N.C. Ct. App. 1984) (allowing recovery for breach of implied warranty by buyer of house with failed septic system against builder of house).

Recovery under implied warranty in the context of a builder's liability is traceable to the 1884 United States Supreme Court decision, Kellogg Bridge Co. v. Hamilton, 110 U.S. 108 (1884). In *Kellogg*, the Court allowed recovery by a railroad company against the company it hired to build a bridge when the temporary supports of the bridge collapsed because the bridge company breached the implied warranty that the temporary supports would be reasonably suitable for the use contemplated by both parties. *Id.* at 118-19.

43. It is true, of course, that the intermediaries hope to keep the benefit of the bargain for themselves rather than pass it on to the purchaser of home. However, that question is the subject of the negotiations between "homeowners" and "developers" over price, warranty, and quality.

44. For example, the court may find that an oversight by the maker of a product led to a defect and the failure of a product, the maker exercised a level of prudence that precluded any claim under implied warranty, even for the initial purchaser. *See, e.g.,* City of Mounds View v. Waljarvi, 263 N.W.2d 420, 424 (Minn. 1978) (refusing recovery under implied warranty against architect when plaintiff's building suffered from water seepage despite fact that builders followed architect's plans because the "inescapable possibility of error which inheres in [architectural] services"). *But see* Broyles v. Brown Eng'g Co., 151 So. 2d 767 (Ala. 1963) (holding defendant civil engineering company liable under implied warranty for occasional failure of drainage system despite lack of evidence of negligence).

Recovery may also be precluded in situations which neither buyer nor seller could have reasonably foreseen the defect in the subject of the transaction. *Compare* Witty v. Schramm, 379 N.E.2d 333 (Ill. 3d App. Ct. 1978) (refusing to imply warranty that no subsurface waters would be present in unimproved building lots and noting neither party had superior knowledge as to existence of subsurface waters) *with* Jordan v. Talaga, 532 N.E.2d 1174 (Ind. 4th Ct. App. 1989) (allowing recovery under implied warranty for buyer of building lot who found property was in natural water course, and was therefore worthless even though seller carried out significant improvements on property, was a professional real estate developer, was in best position to forego development of the lot, and knew of the existence of the natural water course).

When a subsequent purchaser, not in privity with the maker or initial seller, seeks to recover damages caused by a defect in the product, courts may bar recovery unless the subsequent purchaser is endangered in a way that was foreseeable to the initial seller. *Compare* Huang v. Garner, 203 Cal. Rptr. 800 (1st Ct. App. 1984) (allowing recovery under negligence theory by subsequent purchaser of apartment building built by defendant) *with* Stuart v. Coldwell Banker Commercial Group, Inc., 745 P.2d 1284 (Wash. 1987) (refusing recovery from builder under implied warranty to owners of condominium who had no direct

protection for later purchasers is neither absolute nor inevitably sufficient. Its existence, however, calls for rebuttal from the proponents of change.

VI. SOME COSTS OF REFORM

A. *The Uncertainties in the New Body of Law*

Those who would change the rule speak as if tort theory were a fully developed body of law which the courts could transplant to the new factual matrix with little difficulty. The reality is different.

Products liability only recently became a significant branch of the law,⁴⁵ and vital doctrinal questions are still unsettled.⁴⁶ Consider the decades of wrangling over the meaning of "defect" and the extent to which recent proposals for the revision of section 402(a) of the *Restatement (Second) of Torts* have fanned the flames.⁴⁷ In addition, there are disputes as to how the jury should be instructed.

dealings with builder because the defects did not cause a violent occurrence).

45. David G. Owen, *A Highly Blameworthy Manufacturer: Implications on Rules of Liability and Defense of Product Liability Actions*, 10 IND. L. REV. 769 (1977).

The seminal cases that spearheaded the modern development of products liability law were decided in 1960 and 1963. *Henningsen v. Bloomfield Motors, Inc.*, 32 N.J. 358, 161 A.2d 69 (1960); *Greenman v. Yuba Power Prods., Inc.*, 59 Cal. 2d 57, 377 P.2d 897, 27 Cal. Rptr. 697 (1963). The predominant treatise on products liability, L. FRUMER & M. FRIEDMAN, *PRODUCTS LIABILITY* (1976), was first published in 1960, and the first edition of the other treatise in the field, R. HURSH (now with H. BAILEY), *AMERICAN LAW OF PRODUCTS LIABILITY* (2d ed. 1974), was published one year later. The first Canadian text, S. WADDAMS, *PRODUCTS LIABILITY*, was published in 1974, and the first English text has just been published, C.J. MILLER & P. LOVELL, *PRODUCT LIABILITY* (Butterworths 1977).

Id. at 771 n.18.

46. RICHARD A. EPSTEIN, *MODERN PRODUCTS LIABILITY LAW* 69 (1980). Professor Epstein demonstrated design liability embraces fundamentally different categories, and currently the law has not created a rigorous standard for the complex, important cases. *Id.*

Johnson v. General Motors Corp., 438 S.E.2d 28 (W. Va. 1993), is an example of the fluid and unsettled nature of the products liability doctrine. In *Johnson*, claims arising from a head-on collision required the state court to touch on the complexities of "crashworthiness:" the doctrine and the burden of proof in that context; the relationship between one view of the burden and the legislation governing the offsets of settlements; the collateral source rule; the distinction between a defendant's position under a duty to warn based on strict liability and one based on negligence; the "two issue rule;" and other matters. *Id.* at 33-42.

47. Alvin S. Weinstein et al., *Product Liability: An Interaction of Law and Technology*, 12 DUQ. L. REV. 425, 431 (1974).

The meaning or effect of some concepts vary in the different context of tort and contract law. Nothing might seem more familiar or indisputable than the manufacturer's ability to comprehend the nature of the product's probable performance better than the consumer who happens to be hurt in an accident. When the product does not cause physical harm, however, the balance of advantage is the mirror image of those personal injury cases in which strict liability took shape. Now it is the buyer who knows where the product will be used and whether it must act in conjunction with other devices or components. The manufacturer or intermediate seller may *not* know those things; at best, its information comes from the buyer. As a result, the seller has no greater chance to predict the severity of the damage than the buyer.⁴⁸ In fact, quite often the seller has less of a chance.⁴⁹

The change would also burden routine sales with the tort concept of the duty to warn. The impact of that departure would be magnified by the judicial temptation to object to virtually any label or instruction provided for a jury review.⁵⁰ All this clashes with the contractual allocation of risk.⁵¹ Further, those new claims will overlap the warranty rights which purchasers already have.

On a more practical level, if lawyers analyze economic loss cases through the prism of tort theory, they will be encouraged to try them like tort cases. Yet it would not add to the efficiency of commercial life to import more of the theatrics of personal injury litigation.⁵² For example, the plaintiff's tactical reason for pleading tort rather than contract might be to lay the groundwork for a punitive damage count. That, in turn, would bring greater uncertainty as to whether jurors will respond to attacks on the character and morality of the defendant.

48. James A. Henderson & Aaron D. Twerski, *A Proposed Revision of Section 402A of the Restatement (Second) of Torts*, 77 CORNELL L. REV. 1512 (1992).

49. *Id.*

50. It is true that sophisticated buyers often give the seller specific requirements for products, but that is an example of bargaining, the subject of contract law.

51. Courts have recognized that a buyer may consider a "defective" product to be a good bargain if the defect is apparent and reflected in the price. Holding the seller strictly liable in these situations would make these transactions unavailable to consumers and reduce the value of products with patent defects below their true market value. *See* Aronsohn v. Mandara, 484 A.2d 675 (N.J. 1984) (denying buyer of house recovery for defects discoverable upon reasonable inspection, which should have been reflected in price paid); Meadowbrook Condominium Ass'n v. Southern Burlington Realty Corp., 565 A.2d 238 (Vt. 1989) (denying recovery under implied warranty to condominium purchasers, who presumably paid less for their units acquired after defects in common areas became apparent).

52. *See* EPSTEIN, *supra* note 46, at 107 (discussing the lack of unlimited boundaries to liability and the extent to which the duty to warn is also in the midst of development).

B. *The Burden at the Working Level*

These difficulties are not academic curiosities. If the economic loss rule was abolished, trial judges would have to revisit settled issues of contract law in light of tort principles.⁵³ The proposal, after all, is to set up a new universe of precedent. This must be parallel to contract law, but sufficiently distinct from the cases to produce different results in significant cases. Otherwise, there would be no point. Further, the promise of change gives the plaintiff's lawyer a professional duty to contest what once appeared clear.

In turn, those who manufacture and sell goods must foresee the answers courts would give to those questions. Indeed, in many instances the boundaries of the manufacturer's risk would be set by the subjective "expectations" of the purchaser as his or her lawyer chooses to reconstruct them long after the sale. This necessarily reduces the predictability and utility of limitations on warranty or waivers.

Equally important is the fact that producers would have to guess whether another court might decide that a buyer,⁵⁴ or anyone to whom that buyer might resell⁵⁵ the product, lacked "bargaining power."⁵⁶ This

53. See, e.g., *Pennzoil Co. v. Texaco, Inc.*, 481 U.S. 1 (1987) (illustrating the possible dangers judges might face, although the Pennzoil-Texaco situation arose from a different tort theory).

54. Rabin, *supra* note 4, at 1536.

When the ripple effects characteristic of widespread economic loss are involved—that is, the disruption of a heterogeneous conglomeration of commercial and financial relationships occur—the prospect of reasonable foresight is especially attenuated.

Whether this point is equally applicable to the more modest case of widespread economic loss in which physical harm to a particular individual—the running down of a pedestrian, for example—triggers a variety of collateral financial losses, ranging from the victim's boss to his barber, is a closer question. In this situation, however, the relatively weak deterrence claim is arguably outweighed by the ethical objection to extended liability for a careless act.

Moreover, because potentially widespread loss is often either uninsurable or very expensive to insure against, the superior risk-spreading capability of defendants, whether commercial or individual, is open to serious doubt.

Id. at 1536-38.

55. Or anyone else to whom the product might pass later.

56. Variations and asymmetry often exist in individual sales transactions "upstream" and "downstream" from the manufacturer. Contractual bargains up and down the line of production and distribution would be affected by application of a tort theory of liability for the failure of the product to live up to the expectations of the purchaser. Should all suppliers

problem would not be limited to large corporate vendors. Small companies would have the same risk even when they dealt with relatively wealthy individuals.

The "horrible" does not always materialize and in fact cases such as *Greenman* and *Henningsen* did not disrupt commerce.⁵⁷ The reason, however, is not that the danger was imaginary, but that the judges who developed products liability doctrine recognized that tinkering is justified only when the disparity in bargaining power is glaring.⁵⁸ Those who would do away with the economic loss rule have not defined the potential consequences their proposals.

Arguments stating that a change from contract to tort would simplify and rationalize the legal system have vigor and simplicity. But that impression fades upon closer inspection. The supposed reform would actually complicate the liability analysis in some cases.

The distinctions of the principles between strict liability and contractual liability, which is seldom clear in product disputes, grow more blurry when the economic loss case arises from a claim of design defect.⁵⁹ Potential plaintiffs urge that the jury should balance the risk, the costs, and the utility to indicate whether there is a defect. While consumers strike that balance when they decide whether to buy a product or not, jurors could not make more precise judgments after the fact. There also would be a question as to how the jury's finding of a "contract breach" differs from a finding of a defect in an instance where there is no formal agreement.

To be sure, there are important differences between the two bodies of doctrine. However, "different" is not necessarily "better."

of raw materials, contractors, distributors, etc., obtain insurance against liability, limitless in amount, scope, and time? Balancing of the kind required in sales transactions is the function of the U.C.C. and the law of sales, which provide a flexible means by which to measure the proper expectations of all of the parties.

57. Even though it is simpler and less time consuming, classification by category might be inaccurate in many instances. Putting aside the question of fairness, the alternative would be a time consuming, case by case determination of the relative buying powers of the parties. More sophisticated academic writing calls for the analysis of the relationship between the plaintiffs and a determination as to whether or not commercial results will govern. The argument is logical, but as one of its proponent's put it, it would require sophisticated analysis of a variety of cases at the trial level, thus it would be impractical.

58. However, many would argue that those legal developments have had adverse marginal effects on cost and efficiency.

59. See *Brown & Feinman*, *supra* note 10, at 341. Only a very significant difference between the parties' risk-bearing abilities is relevant to the court in its determination of who is the superior risk bearer. *Id.*

VII. THE UNCERTAINTY AS TO WHO WOULD GAIN, HOW, AND WHY

The tort statute of limitations is often shorter than that for contract claims. In addition, the tort action may not survive the death of a party.⁶⁰ Notions of causation are less restrictive in tort law than in contract law⁶¹ and “foreseeability,” already an amorphous concept in contract doctrine, is still less defined in tort law.⁶²

Finally, tort damage principles are often looser than contract damage principles. Contract law gives the claimant the benefit of the bargain rather than compensation for loss.⁶³ Each of the established contract principles developed as courts examined a variety of cases and refined their responses to realities. One of the resulting contract doctrines may be error; all may be mere historical artifacts. Yet before a court accepts either suggestion, it should ask more specific justification for dismantling a system which has evolved over centuries and which permits the doing of the world’s work, no matter how imperfectly.

A. *The Purchaser Without Tears*

Plaintiffs tend to speak as if there was a consensus that the change would help consumers or buyers as a class, and that this is a public benefit so great that compels the abolition of the economic loss rule.⁶⁴

The premise, beguiling so long as its not closely examined, is that a change in the law is desirable if it would make it easier for consumers, or special subcategories of that broad class, to recover for a particular

60. W. PAGE KEETON ET AL., PROSSER AND KEETON ON TORTS 655 (5th ed. 1984).

61. Similarly, immunities such as those of municipal corporations or charities may bar tort claims, but not contract claims.

62. WILLIAM L. PROSSER, PROSSER ON TORTS §§ 42, 92 (4th ed. 1971).

63. *East River*, 476 U.S. at 873-74 n.9.

64. Dean Prosser suggests the tort remedy is often more advantageous to the injured party because it permits the recovery of larger damages, beyond the prototypical limitations of *Hadley v. Baxendale*. KEETON, *supra* note 60, § 9.2, at 665 (citing *Hadley v. Baxendale*, 156 Eng. Rep. 145 (1854)). A tort action may also allow recovery for wrongful death whereas, a contract action would not. *See East River*, 476 U.S. at 874 (placing great emphasis on the distinction between tort and contract).

injury.⁶⁵ The threshold question is whether it *should* be easier for the buyer to prevail under the particular circumstances.⁶⁶

It is debatable whether plaintiffs, as a class, need more help. Newly created implied warranties, condominium legislation and other specialized statutes already have made the balance more favorable for particular groups.⁶⁷ A "reform," giving them additional bargaining power, would help some individual members of those classes win more lawsuits, but it will not always be the plaintiff who gains from the change. For example, to demand proof that the other side was guilty of negligence could make recovery more difficult for some claimants. More generally, traditional warranty law, the U.C.C., and specialized reform statutes, such as lemon laws, provide significant protection for the broad class of "purchasers."⁶⁸ If some need more, the next question is whether the abolition of the economic loss rule is the best way for the courts to help them. Assuredly, there are other paths. Even when codified, general contract and warranty doctrines are flexible enough to allow a court to do justice in the exceptional case. A judge can refuse to enforce an unconscionable contract,⁶⁹ or more specifically, an agreement in which waivers or limitations of liability are so extreme that the remaining remedy fails its essential purpose.⁷⁰

On the other hand, the abolition of the economic loss rule might not make a significant difference to most individuals, or even to a company which has a small claim. In practice, if not in theory, a dispute which involves only property damage at the consumer level cannot often generate

65. The plaintiff's lawyer urging the change in particular cases know what they are doing. Clients would win the individual matters, but that is not enough to justify judicial action.

66. *Mitchell v. Volkswagenwerk, A.G.*, 669 F.2d 1199, 1204 (8th Cir. 1982).

67. That point may seem too obvious to be interesting. Nevertheless, even some academic writing seems to come dangerously close to saying requirements of proof should be abolished for no reason other than they work to the disadvantage of plaintiff. See Gerald F. Teitz et al., *Crashworthiness and Erie: Determining State Law Regarding the Burden of Proving and Apportioning Damages*, 62 TEMP. L.Q. 587, 621 n.21 (1989) (criticizing *Huddell* requirements of proof in "second collision" or "crashworthiness" case because, as long as they remain in force, plaintiff would have to base his or her claim on "speculation or conjecture or both" in instances where an expert can say the design caused the particular harm).

68. See *Casa Clara*, 620 So. 2d at 1247.

69. See U.C.C. §§ 2-313 (express warranty), 2-314 (implied warranty for merchantability), 2-315 (warranty of fitness for a particular purpose) (1994); JAMES L. WHITE & ROBERT S. SUMMERS, *UNIFORM COMMERCIAL CODE* 406 (2d ed. 1980).

70. U.C.C. § 2-302 (1994). See generally WHITE & SUMMERS, *supra* note 69 (discussing related doctrines and remedies).

a contingent fee attractive to the specialized plaintiffs' bar. However, it seems reasonable to expect that most of these cases will be handled as they always have been, by a neighborhood lawyer or the associate who takes his wife's uncle's case in the hope that it will lead to greater things. A typical trial will be a matter of a half-day in a county court, not a venue in which a lawyer often could explore the nuances and complexities of strict liability.⁷¹

The differences will matter, of course, in other cases. Strict liability is more likely to occur in those instances where the litigants have large amounts at stake and have bargained over difficulties which each side foresaw. That brings us full circle to *Seely* and the classical insight that such disputes are the meat and drink of contract law.

VIII. THE FALSE PROMISE OF EXCEPTIONS AND DISTINCTIONS

A. *Assumed Boundaries and Their Life Expectancy*

Insofar as the objective is to shield the individual buyer, the answer might be to preserve the economic loss rule for disputes between corporations or commercial enterprises, but to abolish the doctrine where the plaintiff is an individual. That, however, would mean one rule for businesses and another for those who buy products from these businesses.⁷² The equilibrium could not be stable.

It is the nature of a sales controversy to drag commercial enterprises into what began as simple disputes between private persons or small businesses. For example, when an individual plaintiff obtains a tort verdict against a supplier, builder, or manufacturer, the defendant will usually demand contribution or indemnity from the corporate suppliers further back

71. For an example of a case discussing the complexities of strict liability see *Spring Motors*, 465 A.2d at 530. The essential argument before the Superior Court of New Jersey was that the extension of strict liability would clash with the statutory scheme and was not supported by the policies which underlie strict liability or the weight of authority. *Id.* at 533.

72. Courts more readily apply the economic loss rule in cases in which the plaintiff and defendant are both sophisticated commercial enterprises. Compare *Public Serv. Co. v. Westinghouse Elec. Corp.*, 685 F. Supp. 1281 (D.N.H. 1988) (denying tort recovery to plaintiff company, which sustained losses when steam turbine generator purchased from defendant company malfunctioned) and *Utah Int'l, Inc. v. Caterpillar Tractor Co.*, 775 P.2d 741 (N.M. Ct. App.), cert. denied, 772 P.2d 884 (N.M. 1989) (denying tort recovery to plaintiff company who purchased from defendant company a coal hauling machine which caught fire) with *McConnell v. Caterpillar Tractor Corp.*, 646 F. Supp. 1520 (D.N.J. 1986) (extending tort recovery for economic losses to plaintiff fisherman who purchased boat engine from defendant company).

in the chain of distribution. A comparable dynamic requires that lawyers adapt to the arguments first inspired by the plight of the individual to the needs of ever-larger clients. The cry, in fact, already has gone up that small business also lacks bargaining power.⁷³

IX. SOME DRAWBACKS TO THE "CATASTROPHIC RISK" AND "SEPARATE PRODUCT" EXCEPTIONS

A court may be more receptive to incremental adjustments in the economic loss rule than to a revolutionary change. Problems still lurk beneath the surface. The boundaries of the rule are murky⁷⁴ and they will grow less settled if each case is to require the analysis of the consequences which *might* have come to pass. The ordeal could become a perpetual motion machine, given the impact of the related argument that there should be tort recovery where a product failure is "violent" or likely to create "risks to personal safety."

Plaintiffs struggle to equate their cases to conventional tort claims, crying out against injuries that would have occurred if the product had failed in a different way, and possibly killing or maiming someone. At times, this is only lawyerly melodrama.⁷⁵

Most product failures can be characterized as involving at least a "potential" danger to human life if the plaintiff's attorney has even modest theatrical talent.⁷⁶ That is not a practical limitation on liability, nor one

73. See *Casa Clara*, 620 So. 2d at 1248 (Barkett, J., dissenting); see also *Spring Motors*, 489 A.2d at 677 (Handler, J., concurring) (stating it would not be long before plaintiffs' advocates begin to tell trial courts one company concealed information, and as a result, the other suffered because of its "relative" lack of bargaining power).

74. *East River*, 476 U.S. at 875.

75. In *Bellevue South Associates v. HRH Construction Corp.*, 574 N.Y.S.2d 165, 170 (1991), the Court of Appeals of New York denied recovery in strict products liability for the replacement of a defective floor in residential apartments. The court found no reason to adopt the *East River* rule because the plaintiff failed to meet even a less restrictive test. *Id.* The evidence did not show damage to persons or other property or even risk of such injury from the defective tiles. *Id.* Thus, they were not an inherently dangerous product and the specific failure, delamination of the tiles, was not considered an abrupt, cataclysmic event. *Id.*; see Norman L. Greene, *Away from Ideology: A Review of Product Liability Defenses in the Era of Tort Reform*, 13 PACE L. REV. 43, 75 (1993).

76. In *Casa Clara*, lower grade concrete the buyer purchased led to "spalling," cracking, and staining. It was not unreasonable to extrapolate a situation whereby homeowners found their roofs falling, subjecting innocent people to broken bones, if not death, and as a result, shattering families. The fact that injuries did not actually occur did not make the accounts less blood curdling. *Casa Clara*, 620 So. 2d at 1247.

In *Kodiak Electric Ass'n v. Delaval Turbine*, 694 P.2d 150 (Alaska 1984), the plaintiff electric company sued the maker of a generator that failed, leading to an overload that caused another to fail, and in turn caused an electrical fire. The plaintiff argued that, since it was customary for two workers to go near the unit that caught fire, and since—had they been near it at the time of the fire—they could have been injured, the failure was dangerous, and should trigger tort liability. *Id.* at 153. The Alaskan Supreme Court accepted the argument on the basis of the potential danger to persons. *Id.* at 154. This result is consistent with the Alaskan Supreme Court decision in *Shooshanian v. Wagner*, 672 P.2d 455 (Alaska 1983). Wagner, the general contractor, insulated the plaintiff's building with urea formaldehyde foam insulation ("Insulspray"). *Id.* at 457. The plaintiffs moved into the building, but months later found the Insulspray gave off noxious and malodorous fumes causing allergic reactions and creating a health hazard. *Id.* The plaintiff accused Wagner of negligently installing the insulation, and sought relief because the fumes drove customers away, reducing the value of the building to almost nothing. *Id.* The court permitted the tort claims, holding the plaintiffs' stated a claim upon which relief may be granted under the theories of both implied warranty and strict liability. *Shooshanian*, 672 P.2d at 462-64. The court reached its decision by contrasting *Shooshanian* with an earlier opinion, *Morrow v. New Moon Homes*. *Id.* at 462-64 (citing *Morrow*, 548 P.2d 279 (Alaska 1976)). In *Morrow*, the plaintiffs sued in tort, alleging the mobile home they purchased had a leaky roof, ill-fitting windows and doors, a noisy furnace, and other features that made the mobile home so poor a bargain that they should not pay. *Morrow*, 548 P.2d at 281-82. The *Shooshanian* court contrasted the "poor product" allegation of *Morrow* with the claim in the instant case because the use of the allegedly toxic substance in the building physically altered the structure in a manner rendering it harmful to the plaintiffs. *Shooshanian*, 672 P.2d at 464.

Perhaps, more insightful is the Alaskan Supreme Court's decision *Cloud v. Kit Manufacturing Co.*, 563 P.2d 248, 249 (Alaska 1977), in which dissatisfied mobile home purchasers sued, alleging the polyurethane foam rug padding provided to them as part of the mobile home package ignited, and caused the trailer to catch fire. The Alaskan Supreme Court held the resulting injury constituted "property damage" rather than unrecoverable "economic loss," even though the line between the two is "not always easy to discern, particularly when the plaintiff is seeking compensation for loss of the product itself." *Id.* at 251. The court stated that it could not "lay down an all inclusive rule to distinguish between the two categories; however . . . sudden and calamitous damage will almost always result in direct property damage and that deterioration, internal breakage and depreciation will be considered economic loss." *Id.* (citing Note, *Economic Loss in Products Liability Jurisprudence*, 66 COLUM. L. REV. 917, 918 (1966) [hereinafter *Economic Loss*]). The court provided, as an example, a scenario in which a "defective radiator causes property damage when it results in a fire which destroys the plaintiff's store and causes economic harm because the resulting conditions are so uncomfortable it causes the loss of customer patronage." *Cloud*, 563 P.2d at 251 n.8 (citing *Economic Loss*, *supra*, at 918); *cf.* *Northern Power Eng'g Corp. v. Caterpillar Tractor Co.*, 623 P.2d 324 (Alaska 1981) (categorizing failure of defective oil pressure "shutdown" mechanism that caused engine to stop working as entirely economic loss since other property was not damaged).

The result in *Hiigel v. General Motors Corp.*, 544 P.2d 983 (Colo. 1976), is antithetical to the *East River* doctrine. The plaintiff purchased a motor home from a retailer. The trailer was manufactured and assembled by the Aspen Coach Corporation and mounted on a

Chevrolet chassis manufactured by General Motors. On several occasions, the trailer wheel lug bolts sheared off, causing the dual wheels to fall off the vehicle. Plaintiff sued in strict liability. The trial court dismissed the claim under the economic loss doctrine. *Id.* at 987. On appeal, the Colorado Supreme Court reversed, following *Santor*. *Id.* at 989. "Since under § 402A [of the *Restatement (Second) of Torts*] the burden of having cast a defective product into the stream of commerce falls upon the manufacturer, it appears inconsistent to limit his responsibility to property other than the product sold." *Id.*

In *John R. Dudley Construction Co. v. Drott Manufacturing Co.*, 412 N.Y.S.2d 512 (App. Div. 1979), a construction crane suddenly collapsed. This resulted in serious damage to the crane, but no damage to persons or other property. Holding the event constituted "property damage," the court distinguished *Santor*, reasoning that where there is no physical injury, "it could not be claimed that [the] defendant had committed the tort of marketing a product which contained a defect that made it, when properly used, dangerous to life or limb or property." *Id.* at 515; *see also* *Gainous v. Cessna Aircraft Co.*, 491 F. Supp. 1345, 1347 (N.D. Ga. 1980) (allowing negligence claim for property damage to defective chattel through analysis of analogous cases even though court found no Georgia precedent to distinguish between "economic loss" and "property damage").

Moorman Manufacturing Co. v. National Tank Co., 414 N.E.2d 1302 (Ill. 1980), *rev'd*, 435 N.E.2d 443 (Ill. 1982), focused on a drain storage tank which cracked after 10 years of use. The reviewing court determined this was not the type of sudden, dangerous occurrence best served by tort law policy, rather, the loss was seen as "commercial," a type best handled by contract. *Id.* at 450. Justice Moran expressed the majority view as follows: When "the harm relates to the consumer's expectation that a product is of a particular quality so that it is fit for ordinary use" and the defect is of a qualitative nature, contract law is appropriate. *Id.* at 451. To hold the manufacturer "strictly liable in tort for the commercial loss suffered by a particular purchaser, it would be liable for business losses of other purchasers caused by the failure of the product to meet the specific needs of their business." *Id.* at 447. The majority rejected the suggestion that if there is any physical harm, all losses should be recoverable. *Id.* at 452. The concurring opinion suggested that in some instances, plaintiffs could recover, even in the absence of privity. *Moorman*, 435 N.E.2d at 456 (Simon, J., concurring). Obviously, the question does not allow for a uniform answer. The proper approach is to develop a system of warranties out of privity to protect warranty-like, that is contract-like, interests, while resorting to tort theories to protect tort interests.

In *Prairie Production, Inc. v. Agchem Division-Pennwalt Corp.*, 514 N.E.2d 1299 (Ind. Ct. App. 1987), economic losses were not recoverable by a seed corn grower on the basis of a negligence claim against the manufacturer of a pesticide that failed to eliminate corn earworms leading to lost profits. The reasoning emphasized a claim for lost profits was purely economic in nature, and therefore recovery was limited to contract. *Id.* at 1304. Further, to allow recovery of economic losses in a tort-based claim would circumvent the legislative framework set forth in the U.C.C. *Id.* at 1304-05; *see also* cases cited *supra* note 72.

In *Detroit Edison Co. v. Nabco, Inc.*, 35 F.3d 236 (6th Cir. 1994), Detroit Edison, a utility company, filed suit against Dravo Corporation and Vectura Group, Inc. (collectively, "Dravo") for damages resulting from the explosion of a 40 foot section of hot reheat pipe located in a power producing unit. Dravo fabricated and supplied all of the reheat pipe to Detroit Edison. Detroit Edison sought damages in tort for over \$20 million in damages for

which sellers could evaluate in advance. A part of the truth may be that the humanitarian basis of the product liability revolution decays into bombast when the claim is only for property damage.⁷⁷

the cost of repairing or replacing the defective pipe and surrounding machinery; repairing other machinery and property damaged by the explosion; cleaning up and removing the asbestos insulation used on the reheat pipe; inspecting all of the reheat pipe; purchasing replacement power from other utility companies while the damaged power unit was repaired and inspected and while other units were operating at a reduced capacity to minimize the risk of another explosion. *Id.* at 238. Following *Neibarger v. Universal Cooperatives, Inc.*, 486 N.W.2d 612 (Mich. 1992), the trial court granted summary judgment for the defense, holding that all of Detroit Edison's tort claims were barred under the economic loss doctrine. *Detroit Edison*, 35 F.3d at 238. On appeal, the Sixth Circuit affirmed, holding:

[The rule which] emerges from *Neibarger* significantly narrows the "other property" exception while expanding the definition of economic loss. Under *Neibarger*, tort claims for damage to other property are barred by the economic loss doctrine if those losses are direct and consequential losses that were within the contemplation of the parties and that, therefore, could have been the subject of negotiations between the parties.

Id. at 241 (citing *Neibarger*, 486 N.W.2d at 620). The Sixth Circuit reasoned the Michigan Supreme Court "significantly curtail[ed] the applicability of the 'other property' exception to the economic loss doctrine, while [simultaneously] expanding the meaning of 'economic loss.'" *Id.* at 243.

77. See, e.g., *Pennsylvania Glass*, 652 F.2d at 1165 (holding seller of front-end loader liable in tort for defect that caused loader to catch fire, despite fact that it only damaged itself because fire was sudden and calamitous); *Gainous*, 491 F. Supp. at 1345 (extending tort recovery to buyer of plane which malfunctioned in midflight, necessitating emergency landing resulting in damage to only airplane); *Shooshanian*, 672 P.2d at 455 (holding tort recovery was available to buyer of product with dangerous defect, regardless of suddenness of product's failure); *Northern Power*, 623 P.2d at 324 (denying recovery to buyer of generator that seized because there was no evidence of damage to persons or property, and failure created no risk to persons or property); *Cloud*, 563 P.2d at 248 (categorizing damage resulting from fire caused by polyurethane foam rug padding included in mobile home as recoverable "property damage," and noting that sudden and calamitous damage is generally put in this category, while deterioration, internal breakage, and depreciation are generally considered economic loss); *Moorman*, 435 N.E.2d at 443 (refusing recovery under strict liability by buyer of grain storage tank that developed crack which buyer did not discover until months later, and distinguishing cases in which defect causes violence or collision with external objects); *Drott*, 412 N.Y.S.2d at 512 (holding construction crane that suddenly collapsed created "property damage," despite fact that it only damaged itself, because it was dangerous to life or property); *Economic Loss*, *supra* note 76, at 917 (arguing defective radiator that causes fire and destroys plaintiff's store causes economic harm, while radiator that creates uncomfortable conditions that leads to drop in patronage causes only economic loss).

Courts may be more inclined to treat loss which is essentially economic as property damage when the defect at issue creates severe inconvenience for the buyer, even when it threatens damage only to itself. In *Hiigel*, the Colorado Supreme Court extended tort

In other instances, however, the evidence does suggest a genuine risk. Where the injuries are tangible, it is difficult to quantify the risk in a mass-produced product. Where an accident does not occur, the risk itself becomes indistinguishable from the rhetorical effects which the attorney creates. And even here, those who would change the rule fail to trace the link between premise and conclusion.

Under traditional law, if negligence or a product defect creates a danger and yet does no harm in the specific instance, there is no tort.⁷⁸ Opening that gate would give anyone who “might” have been hurt a right to sue—an idea that courts have rejected for centuries.⁷⁹

At first glance the contention that a defective product is “separate” from other components of a building or complex machine⁸⁰ may seem to make more sense.⁸¹ But hours, if not days of threshold testimony must

recovery to the buyer of a motor home trailer that had to be tested to assess the level of torque pressure at particular intervals of mileage driven. *Hiigel*, 544 P.2d at 988.

78. See, e.g., *A.J.P. Contracting Corp. v. Brooklyn Builders Co.*, 11 N.Y.S.2d 662 (Sup. Ct. 1939), *aff'd*, 28 N.E.2d 412 (N.Y. 1940); *MacPherson v. Buick Motor Co.*, 111 N.E. 1050 (N.Y. 1916) (refusing tort recovery when the defective product did not cause injury or property damage).

79. See *Harris v. Forklift*, 114 S. Ct. 367 (1993) (Scalia, J., concurring).

80. See, e.g., *Northridge Co. v. W.R. Grace & Co.*, 471 N.W.2d 179 (Wis. 1991). In *Northridge*, the owners of two shopping centers brought suit against the builder of the shopping malls. Plaintiff purchased the asbestos product directly from the general contractor, not from the manufacturer. *Id.* at 180. The owners apparently thought they had some kind of warranty claim because they sued for breach of warranty, as well as under several tort theories. *Id.* Plaintiffs claimed the material was defective and unreasonably dangerous; they incurred increased expenses for inspection, testing, and removal of the material; and they suffered diminished value of the properties upon sale. *Id.* The fire coating manufacturer successfully argued the only damages claimed for economic loss arose from a perceived problem with the material itself, and thus, recovery on the tort claims was barred. *Id.* The circuit court also held that any warranty claim was barred by the statute of limitations, and it dismissed the action. *Northridge*, 471 N.W.2d at 180. The Supreme Court of Wisconsin accepted a petition for bypass and reversed. *Id.* On appeal, the plaintiffs did not argue the material failed to perform as expected, but rather the asbestos in the product contaminated the shopping centers, thereby damaging property other than the product itself. *Id.* The defendant argued that the plaintiffs did not allege any damage to such property other than the reduced economic value of the other property resulting from the mere presence of the material. *Id.*

81. In *East River*, the Supreme Court pointed out the complex nature of modern industrial products would make the rule meaningless if it were limited to individual components. *East River*, 476 U.S. at 871. *East River* was decided under admiralty law. Therefore, one might posit its holding as non-binding on state courts or even on federal courts in non-admiralty cases. Nevertheless, the opinion appears persuasive, wholly aside from Justice Blackmun's analysis beginning with the premise that admiralty law incorporated

drag by as plaintiffs try to prove the “separable” nature of each “product” or component.⁸²

general principles of product liability law. *Id.* at 863.

In *King v. Hilton-Davis*, 855 F.2d 1047 (3d Cir. 1988), *cert. denied*, 488 U.S. 1030 (1989), the Third Circuit considered the “separability” of a product under *East River*. The plaintiff farmers purchased seed potatoes which failed to germinate when they were treated by another farmer with a chemical manufactured by the defendant. *Id.* at 1049. The plaintiffs premised their tort claim on the idea that the chemical and the seed potatoes were separate products. Since the chemical damaged the seed potatoes, the “product” did not “injure only itself” for the purposes of applying *East River*. *Id.* at 1051. The jury found for the plaintiffs because Hilton-Davis failed to warn the plaintiffs of the properties of the chemical that caused the failure. *Id.* at 1049. The Third Circuit reversed, holding the relevant “product” in the context of the *East River* rule is the product purchased by the plaintiffs (the treated seed potatoes), rather than the product sold by the defendant (the chemical). *Id.* at 1051. Thus, the “product” involved in the case “injured only itself,” and under *East River*, the plaintiff farmers were limited to the warranty provided by the seller of the treated seed potatoes. *King*, 855 F.2d at 1051.

The Alaska Supreme Court rejected a separability argument in *Northern Power & Eng’g Corp. v. Caterpillar Tractor Co.*, 623 P.2d 324 (Alaska 1981). In that case, a low oil pressure shutdown mechanism in a tractor failed, causing the engine to overheat and seize. The plaintiff argued the shut-down mechanism damaged another “component part” of the engine, and thus caused the property damage. The court rejected this “separate product” argument in cases where the components are provided by one supplier as part of a complete and integrated package. *Id.* at 330. “Since all but the very simplest of machines have component parts, such a broad holding would require a finding of ‘property damage’ in virtually every case where a product damages itself. . . . [and would] eliminate the distinction between warranty and strict products liability.” *Id.*

Separability issues also arise in the context of construction projects, which combine the “products” of architects, engineers, suppliers, subcontractors, and general contractors. Even the completed building may be separable from the property on which it is located, as the plaintiffs in a 1983 Montana case argued. *See Chubb Group of Ins. Cos. v. C.F. Murphy & Assocs., Inc.*, 656 S.W.2d 766 (Mont. 1983) (allowing recovery from builders of arena under strict liability when arena collapsed because value of leasehold, a separable piece of property, reduced).

82. *Tony Spychalla Farms, Inc. v. Hopkins Agric. Chem. Co.*, 444 N.W.2d 743, 747 (Wis. Ct. App. 1989). In *Spychalla*, a potato farmer brought a strict liability action against the manufacturer of a dust designed to prevent potatoes from rotting. As a result of applying the dust, the farmer’s potatoes petrified. The plaintiff did not claim the manufacturer’s potato dust failed to prevent the potatoes from rotting. Rather, the plaintiff claimed that the product actually injured the potatoes by causing them to petrify. The *Spychalla* court recognized an exception to the economic loss doctrine, finding it inapplicable where an allegedly defective product caused actual damage to other property. *See also D’Huyvetter v. A.O. Smith Harvestore Products*, 475 N.W.2d 587 (Wis. Ct. App. 1991). Farmers brought suit against the manufacturer and retailer of a “Harvestore” system. A “Harvestore” system is a large grain silo for preserving and storing feed for livestock. Among the plaintiffs’ claims against the manufacturer and retailer were claims of negligence and strict liability. The trial court

There would also be a less tangible cost: the decline of the moral authority of the trial system.⁸³ In a building product controversy, for example, the judge could conclude that the seller of concrete would be liable to the buyer of a house.⁸⁴ In a different court, the holding might be that

granted summary judgment for the defendants, because the only losses were economic. On appeal, the plaintiffs contended that the alleged defective nature of the Harvestore system caused damage to feed stored in the system and to their livestock. They contended this constituted damage to other property. The court rejected the plaintiffs' arguments, finding their alleged damages were economic losses not exempted by the "other property" exception. *Id.* at 595. The court stated, "[t]he expected function of the Harvestore was to enrich the feed, providing enhanced nutrition for the cows. The damages stem from the failure of the Harvestore to perform 'as expected,' . . . and not from 'injury to another person or property.'" *Id.* (quoting *Tony Spychalla Farms, Inc. v. Hopkins Agric. Chem. Co.*, 444 N.W.2d 743, 746 (Wis. Ct. App. 1989)).

83. James A. Henderson, Jr., *Judicial Review of Manufacturers Conscious Design Choices: The Limits of Adjudication*, 73 COLUM. L. REV. 1531, 1542 (1973).

84. Commentators trace the modern basis of the builder's liability to *Kellogg Bridge Co. v. Hamilton*, 110 U.S. 108 (1884). The bridge company agreed to build a bridge for the railroad. The work began with the construction of "false work" (essentially platforms) in the river. The company contracted with Hamilton to finish the work. Hamilton paid the company for the work completed until that point. The "false work" inadequate and one platform sank under the weight of the bridge. River currents destroyed a second platform. Hamilton sued and recovered damages for the defective structures. The Supreme Court held the bridge company made no representations as to the "false work" in place, but found it portrayed itself as competent enough to build such structures. *Id.* at 117. The deficiencies in the "false work" were unknown and undiscoverable until the foundations were subjected to practical testing in the course of construction. Under those circumstances, the Court held the bridge company breached an implied warranty that the "false work" would be "reasonably suitable" for such use as was contemplated by both parties. *Id.* at 119. The *Hamilton* court relied on analogies to warranties implied in the sale of goods and treated the transaction at issue as a "sale" of the "false work" by the bridge company to Hamilton. The Court stated:

[The false work] was constructed for a particular purpose, and was sold to accomplish that purpose; and it is intrinsically just that the company, which held itself out as possessing the requisite skill to do work of that kind, and therefore as having special knowledge of its own workmanship, should be held to indemnify its vendee against latent defects, arising from the mode of construction, and which the latter, as the company well knew, could not, by any inspection, discover for himself.

Id.; see William K. Jones, *Economic Losses Caused by Construction Deficiencies: The Competing Regimes of Contract and Tort*, 59 U. CIN. L. REV. 1051 (1991) (suggesting Hamilton's theme was reiterated a century later in *Hartley v. Ballou*, 209 S.E.2d 776 (N.C. 1974)). In *Hartley*, the basement of the dwelling, which Hartley purchased from the builder, flooded during rainy weather. Ballou, the builder, made extensive repairs, and as a result the basement stayed dry during hurricanes and periods of extraordinarily heavy rain. The court held the buyer could recover his damages from the initial flooding, but not for damages associated with subsequent episodes. *Hartley*, 209 S.E.2d at 776. The implied warranty only

applied to latent defects, not to those which would be visible on reasonable inspection of the dwelling. Moreover, the implied warranty was not an absolute guarantee against flooding in the event of hurricanes or other extreme weather conditions. *See also* *George v. Veach*, 313 S.E.2d 920 (N.C. 1984). In *George*, the builder breached the implied warranty that a residential home would be fit for human habitation when the septic system failed. The court opined that the implied warranty imposed strict liability on the warrantor. *Id.* at 922. Professor Jones criticizes this decision, suggesting that the failure of the septic tank was no more than an “economic loss”—a diminution in the value of the purchased property not accompanied by injury to person or other property. Jones, *supra*, at 1056. While Professor Jones recognizes holdings of economic loss as an inappropriate basis for an action in tort, he urges the matter requires further analysis and not mere analogy. *Id.* Thus, he suggests the court was correct in referring to an “asymmetry” in the information available to the buyer and the seller. The seller is in a better position than the buyer to learn of the defects or the potential defects. The buyer could hire experts and conduct inspections to test the soundness of the property to be purchased, but the buyer and his experts are not normally present during the construction when most of the information about any defects is not hidden from view. Moreover, Jones suggests it is socially wasteful to impose an obligation on the buyer to do extensive tests to learn what the seller already knows or could have easily ascertained. *Id.*; *see also* *City of Mounds View v. Walijarvi*, 263 N.W.2d 420 (Minn. 1978) (refusing to apply such a warranty in suit against an architect, although recognizing the city could sue a building contractor for such a defect). The *City of Mounds* court noted that:

Architects . . . deal in somewhat inexact sciences and are continually called upon to exercise their skilled judgment in order to anticipate and provide for random factors which are incapable of precise measurement. . . . Because of the inescapable possibility of error which inheres in these services, the law has traditionally required, not perfect results, but rather the exercise of that skill and judgment which can be reasonably expected from similarly situated professionals.

Id. at 424; *see also* *Huang v. Garner*, 203 Cal. Rptr. 800 (1984) (denying recovery in warranty, yet permitting recovery under negligence theory emphasizing: 1) foreseeability of harm to purchaser; 2) extent to which transaction was meant to effect plaintiff; 3) certainty that plaintiff suffered injury; 4) closeness of connection between defendant’s conduct and injury suffered; 5) moral blame attached to defendant’s conduct; and 6) policy permitting future harm); *COAC, Inc. v. Kennedy Eng’r, Inc.*, 136 Cal. Rptr. 890 (Cal. Ct. App. 1977) (holding engineer’s contract with water district made successful project bidder intended beneficiary, permitting it to sue engineer in contract for damages suffered when engineer prepared documents in late and defective manner); *Witty v. Schramm*, 379 N.E.2d 333 (Ill. App. Ct. 1979) (refusing recovery for breach of implied warranty of habitability for discovery of subsurface waters that hampered construction because neither party has such knowledge and no one was at fault); *cf.* *Broyles v. Brown Eng’g Co.*, 151 So. 2d 767 (Ala. 1963) (permitting an implied warranty claim against a civil engineer who warranted the “sufficiency and adequacy of the plans and specifications to reasonably accomplish the purpose for which they were intended” and distinguishing engineering work from the professionalism at issue in *City of Mounds*, reasoning it is far less subject to factors beyond the control of the professional); *A.R. Moyer, Inc. v. Graham*, 285 So. 2d 397, 402-03 (Fla. 1973) (rejecting premise that design professional’s contract was intended to benefit any one other than contracting parties absent clear intent of parties as evidenced by terms of contract); *Jordan*

the seller of plywood or electrical wiring is not subject to tort claims because it is a separate product. Each ruling could follow from characteristics which one judge thought critical on that particular day and in that particular context. But the public would not have faith in a principle of law which produced different outcomes in similar transactions.

X. WHO IS THE HAND AND WHO IS THE EYE?

Whether or not it is wise, the impetus for change arises from a humane impulse. But at what point must the courts leave those profound matters to the elected branch? We add little to the vast literature on that question,⁸⁵ other than to say that product liability law is notoriously vague. The task of trial judges and intermediate appellate courts is to decide a particular case on a relatively traditional, limited nature, such as the existence of a statute of limitation, a waiver, or the particular product's failure, regarding the adequacy or inadequacy of a defect. If the economic loss rule were to vanish or weaken significantly, even these islands of certainty in the product liability sea would shrink. Judges would have to operate on a border between law, technology, and public policy. They would have no guidance other than benign emanations from earlier, different cases which had dealt with clear-cut injustices and a demonstrated need for action.

There is more at stake, remember, than technical jurisdiction. A broad shift away from contract principles must clash with the constitutional ideal of comity between the branches of the government.

In the past decade, state legislatures have enacted a wide variety of tort reform measures.⁸⁶ Their common denominator is the intent to cut back the scope of liability and to impose specific limitations on key aspects of damages. The courts would mock that legislative initiative by broadening tort liability and creating difficult new issues of damages across an already ill-defined spectrum.

v. Talaga, 532 N.E.2d 1174 (Ind. Ct. App. 1989) (holding seller breached implied warranty where it was later determined flooding was so prevalent in area that house he built was worthless and emphasizing: 1) seller had subdivided land; 2) seller was real estate development professional; 3) seller was in better position to leave lot undeveloped and, hence, absorb losses; and 4) seller knew of natural water course and was in better position to use information).

85. The courts regard controversies of that type as the constitutional prerogative of the legislative branch. See generally MORTON J. HOROWITZ, *THE TRANSFORMATION OF AMERICAN LAW 1870-1960: THE CRISIS OF LEGAL ORTHODOXY* (1992).

86. *Smith v. Department of Ins.*, 507 So. 2d 1080 (Fla. 1987).

There are considerations of institutional expertise and resources as well. The proponents of change do not quantify the costs of their proposal, or the economic impact that the shift in the doctrine would have. For that matter, they offer little data as to the number of cases which would be decided differently,⁸⁷ or even specifics as to how the new results would be fairer, or more socially beneficial. To the extent a court accepts those arguments, it acts on the basis of predictions of social consequences which are essentially guesswork.

At some stage, even necessary guesses, educated or irresponsible, become indistinguishable from managerial or political decisions. If that lack of information were unavoidable, courts might have to act in partial ignorance for the sake of doing justice. There is no such necessity. Other constitutional branches have the resources to gather data and to assess the merits of competing solutions.

The legislative staff's function is to gather expert opinions concerning technical and economic factors.⁸⁸ Equally important, is the legislators' ability to focus on a particular question and formulate a remedy that is tailored to broad social needs rather than the plight of an isolated litigant.⁸⁹ At the level of implementation, federal and state agencies, rather than an individual attorney, can make a more realistic and fair evaluation of the costs and benefits to both individuals and the public.

XI. THE POSSIBILITY OF LESS DISRUPTIVE ALTERNATIVES

The prominent issue of contract or tort tends to obscure the important technical questions. For instance, one commentator has suggested that since building contractors are prone to bankruptcy, a shift to a tort doctrine would

87. Returning to the construction cases, plaintiffs have often brought lawsuits against their builders, general contractors, and architects. They do not tell the courts why those suits, each permissible under existing law, would not give them reasonable compensation for whatever losses they may have suffered.

88. Bills are accompanied by a statement of economic impact to aid the legislative staff in this task. *See* FLA. STAT. § 11.075 (1993).

89. If the object is to govern future conduct, the task may be accomplished better through administrative regulations or statutes, each of which expresses public goals arrived at by the public's elected representatives or their deputies. This ideal may not be achieved in every instance, but the serious question is whether the task should be entrusted to judges or even juries, neither of which are elected. Note, it is common for economic loss rule controversies to arise in the context of regulated industries. *See* Florida Power & Light Co. v. Westinghouse Elec. Corp., 510 So. 2d 899 (Fla. 1987).

reduce the danger for the ultimate purchasers of building materials.⁹⁰ Legislators could enact statutory reform, focusing more closely on the specific problem,⁹¹ such as an increase in the performance bond requirement. That approach, tailored to the individual problem, would be both more effective and less dangerous than a sweeping change from a contract to a tort doctrine.⁹²

As another example, the objections and difficulties previously discussed might be brought under control if the reform impulse were expressed through the abolition of the vertical privity requirement in existing warranty law.⁹³ The effect would be to put the buyer in the same position as a sophisticated commercial purchaser. This would be consistent with both traditional law and the expectations which a business has in launching a product. On the other hand, the change would not undermine express waivers or limitations of warranty. Nor would it subject sellers to unmeasured damages.

The question, however, is not an easy one.⁹⁴ The authors suggest that it should be addressed only on its own merits. If treating the validity of a privity requirement is dependent upon a philosophical debate over the virtues of contract and tort law, then neither side is likely to reexamine the policy aspects of the particular question. Such an examination, supposedly, is a hallmark of modern law.⁹⁵

90. Michael D. Leider, *Constructing a New Action for Negligent Infliction of Economic Loss: Building on Cardoza & Coase*, 66 Wash. L. Rev. 937, 1016 (1991).

91. Compare the specific reforms in various recent tort reform statutes such as Florida's Tort Reform and Insurance Act of 1986. See *Smith*, 507 So. 2d at 1080.

92. Indeed, the California Supreme Court made precisely those limited adjustments in *Seely*. The policy in product liability analysis is to advance the interests of plaintiffs by resolving future issues in favor of the plaintiff.

93. In fact, that was the approach the New Jersey court took in *Spring Motors*. The change in existing law would not be radical. The U.C.C. is neutral as to the vertical privity requirement. See section 2-318 and the express statement in the comments to this section explaining that the provision is not meant to limit the "developing case law" which tends to diminish the requirements of privity. See *Parker*, *supra* note 4, at 410.

94. See *WHITE & SUMMERS*, *supra* note 69, § 11-5, at 463 (exemplifying buyer who obtains goods secondhand from intervening vendor to support that the question is debatable and consequential economic losses should be denied to buyer not in privity).

95. The closer the focus, the better. If the basic fact pattern is characterized as a question of privity, there are overtones of archaic learning that cut off the rights of the buyer for no practical purpose. On the other hand, when the general idea is expressed in terms of the absence of face-to-face dealings and the lack of opportunity for either side to bargain, the fundamental considerations seem more appealing.

XII. GOALS OR ANALYSIS

“General propositions do not decide concrete cases.”⁹⁶ The proposal that the economic loss rule be abolished endures, in part, because judges and attorneys have been conditioned to think of the expansion of product liability as the path of the future. Moreover, they give exaggerated deference to insights which were appropriate to the pioneering decisions. In a sense, they confuse the ends of product liability law with the means. Our thesis is not that those insights are necessarily wrong or outdated, but that they cannot effectively provide the tools for the analysis of every controversy.

A. Compensation

To say compensation for an injured party is a traditional objective of tort law⁹⁷ is not to demonstrate that the buyer should recover in tort.⁹⁸ Rather, in its more brutally direct form, the argument is that the change would make it easier for the plaintiff to win. But that would be an effect, not a reason. The change in the balance of power cannot be a policy argument in and of itself.

There is a need for a closer and more skeptical look at the related suggestion that courts should give homeowners, fishermen, or any other category of litigant favored treatment across the board. In other fields of law, the starting point for analysis is not the status of the claimant⁹⁹ but the circumstances of the individual matter. The impulse reflects the belief that “homeowners,” as well as other groups, suffer from a disparity in bargaining power. Accordingly, the courts can and should correct this imbalance. However, there are flaws in the syllogism. If it were taken literally, the contention would mean courts should find for homeowners in every other instance, regardless of facts or law. There are few cases in which the individual buyer would have “greater bargaining power” over a corporate

96. *Lochner v. New York*, 198 U.S. 45, 76 (1905) (Holmes, J., dissenting).

97. See RICHARD A. POSSNER, *ECONOMIC ANALYSIS OF LAW* § 20 (4th ed 1988).

98. See generally Christopher D. Stone, *The Place of Enterprise Liability in the Control of Corporate Conduct*, 90 YALE L.J. 1 (1980). The author notes “risks of over deterrence are heightened when there is no certain expenses, such as the installation of known technology, that will avoid the liability with certainty.” *Id.* at 25-26. Similarly, the conclusory statement that the buyer’s expectations were not met does not identify a test which trial courts could apply. Often it is only a label for the result reached for other unstated reasons.

99. See *J’Aire Corp. v. Gregory*, 598 P.2d 60 (Cal. 1979) (proposing that the circumstances, not the status of the claimant controls).

seller.¹⁰⁰ In any event, the leading cases agree that relative bargaining power is not the touchstone of the economic loss rule, nor even an element.¹⁰¹ And were the law different in principle, trial judges would still face difficulties.

The concept of relative bargaining power is itself indistinct and subjective. It is a function of talent, resources, luck and other intangibles inherent in a vast array of relationships. Leading cases such as *Spring Motors* and *Seely* show that judges who lead the charge for product liability can differ in their evaluation of the balance of power even where the business relationships are relatively straightforward.¹⁰²

Beyond that, reliance on "policy" combines with limitations inherent in the trial process itself to make the assessment of relative bargaining power a rudimentary exchange for lawyers' arguments based upon stereotypes. Delphic rulings by trial judges denying or granting summary judgment without explanation could offer little or no precedent for the next case, much less guidance to business.

100. The occasional Astor who lost an eye to a champagne cork would not make the generality invalid. See David G. Owen, *Rethinking the Policies of Strict Products Liability*, 33 VAND. L. REV. 681 (1980) (criticizing the "one directional" nature of other arguments which frequently are offered in support of plaintiff oriented proposals for changes in products liability law); see also Edward T. O'Donnell, *Public Policy and the Burden of Proof in Enhanced Injury Litigation: A Case Study in the Dangers of Trends and Easy Assumptions*, 17 W. ST. U. L. REV. 325 (1990); David G. Owen, *Products Liability: Principles of Justice for the 21st Century*, 11 PACE L. REV. 63 (1990) (elaborating on the same theme).

101. In *Spring Motors*, the court sometimes spoke of equal bargaining power and the ability to spread the loss as prerequisites to contract. *Spring Motors*, 489 A.2d at 670-71. The New Jersey Supreme Court specified "perfect parity is not necessary to a determination that the parties have substantially equal bargaining positions," and further, a commercial purchaser "may be better situated than the manufacturer to factor into its price the risk of economic loss caused by the purchase of a defective product." *Id.* at 671. Thus, if commercial purchasers miscalculate their risk when bargaining for their contract or err in risk allocation by not purchasing appropriate insurance, the consequences are not to be borne by the manufacturer under a false or fictitious tort theory. The law of warranty is not limited to parties in a somewhat equal bargaining position. Such a limitation is not supported by the language and history of the sales act and is unworkable. Moreover, it finds no support in *Greenman v. Yuba Power Products, Inc.*, 377 P.2d 897 (Cal. 1963).

102. The fact the dealership could select a Clark transmission for the Ford trucks it bought showed significant bargaining power to some members of the court, but to another member of the court, the same facts showed the manufacturer only chose to make the component available as an option. See *Spring Motors*, 489 A.2d at 678 (Handler, J., concurring); see also Brown & Feinman, *supra* note 10, at 348-59 (discussing the thoughtful debate between the majority and concurring opinions and the academic benefits of relational analysis).

B. Deterrence—Goal or Mirage?

Plaintiffs suggest that giving property holders the right to sue in tort rather than contract would advance the cause of product safety. Their premise is that existing law does not give an owner reason to repair dangerous conditions before an accident occurs. On the contrary, the opposite is true. A property holder knows full well that he or she may be sued if someone is injured on the premises. In *Casa Clara*, for instance, each of the corporate amici,¹⁰³ which supported the plaintiffs, took care to assure the appellate court that its workers had repaired the roofs in dispute before the company sought legal remedies against suppliers further back in the distribution chain. There is no reason to think other businesses, equally public spirited, or just as worried about their products' reputation, would not have taken similar precautions.

On the other hand, at least one consequence of a shift from contract to strict liability is clear. The change would tell manufacturers that greater care would not be a defense.¹⁰⁴ Then, where lies the incentive for those businesses to take greater care?

One of the early critics of the economic loss rule, Justice Peters, remarked that the threat of a strict liability claim could not be a significant deterrent to businessmen who already know that they are subject to suits for negligence or breach of contract.¹⁰⁵ On similar lines, it is significant that the product liability revolution has reduced qualitative standards of proof of causation and defect.¹⁰⁶ The purpose and effect of that change is to make it easier for plaintiffs to recover. But the same dilution of proof must make it more difficult for a manufacturer to interpret society's message. The product should have been safer, but in what way and at what cost?¹⁰⁷

103. The reference is to those participants who joined in the attack on the economic loss rule.

104. Strict liability subjects the seller to judgment even if the seller "has exercised all possible care in the preparation and sale of his product" RESTATEMENT (SECOND) OF TORTS § 402(A)(2)(a) (1965).

105. *Seely*, 403 P.2d at 152-58 (Peters, J., concurring in part & dissenting in part).

106. *Barker v. Lull Eng'g Co.*, 573 P.2d 443 (Cal. 1978); Edward T. O'Donnell, *Design Litigation and Strict Liability: The Problem of Jury Instructions Which Do Not Instruct*, 56 U. DET. J. URB. L. 1052 (1979).

107. See generally Edward T. O'Donnell, *Design Litigation and the State of the Art: Terminology, Practice and Reform*, 11 AKRON L. REV. 627 (1978).

C. *Higher Prices—The Skull Behind the Mask*

Eventually, arguments for the expansion of tort remedies will lead to the development of a system in which product liability costs can be shared among all consumers through higher product prices. Familiar and reassuring as the litany may be, it goes too far. If that were all there were to it, every product liability issue would be decided in favor of a plaintiff. The change must increase the number of lawsuits—and the costs of insurance and the products themselves—if it is to serve its doctrinal purpose. Isolated and infrequent cases could not distribute the loss effectively.

And, in ordinary speech, higher prices are not a public benefit. When prices go up, fewer people can buy goods and the manufacturer must restrict its production and lay off workers. Given that reality, it is not self-evident why hypothetical buyers need a tort remedy, in addition to the contract rights they already possess. Nor is it clear that a court would help even favored groups such as potential home owners, if it were to take steps leading to an increase in the prices of building materials. The ordinary citizen would have to make a larger down payment in order to buy a home. Many would not be able to do so.

D. *Insurance and the Sharing of Pain*

A more abstract and sophisticated variant, the concept of the manufacturer as a superior risk distributor,¹⁰⁸ has gained numbing force through repetition.¹⁰⁹ Yet Dean Prosser terms this a “make weight,” even as to personal injury.¹¹⁰ Other commentators¹¹¹ point out that the reasoning, if valid, must apply whenever anyone is injured by a superior risk-bearer, and that logic would call for a governmental compensation scheme for all

108. See *Emerson G.M. Diesel, Inc. v. Alaskan Enter.*, 732 F.2d 1468, 1474 (9th Cir. 1984); *Jones & Laughlin Steel Corp. v. Johns-Manville Sales Corp.*, 626 F.2d 280 (3d Cir. 1980).

109.

The manufacturer knows the purpose for which its product is to be used and by whom. Although all purchasers are not identical, the manufacturer can determine within a reasonable range of predictability the ramifications of a product failure for the ordinary user. Having this information, the manufacturer can include in its cost the expense of adequate insurance coverage.

Emerson, 732 F.2d at 1474.

110. William L. Prosser, *The Fall of the Citadel (Strict Liability to the Consumer)*, 50 MINN. L. REV. 791, 799-800 (1966).

111. See Owen, *supra* note 100, at 707.

resulting injuries. That formulation is extreme, to the point of being a caricature, and not what the proponents of the change desire. However, bounds have not yet been set to prevent well-intentioned reforms from surging beyond their original purposes. Instead, the arguments for risk distribution dwindle toward assertions that the law could be changed without hardship.

The magical painkiller is said to be "insurance." Yet, courts have assured manufacturers and other defendants a thousand times that they will not be subjected to an insurer's liability.¹¹² That language must degenerate into incantation if judges now were to create a whole new spectrum of liabilities on the basis that defendants could buy insurance.¹¹³

To be fair, it is not only plaintiffs' advocates who have been lulled by superficial talk of insurance. In *East River*, Justice Blackmun supported his refusal to alter the economic loss rule by writing that the seller of a product could buy insurance against liability. The observation gained resonance from its seeming consistency with product liability lore. Yet on closer inspection, there is no difference between tort and contract to the extent that the question is one of theoretical insurability.¹¹⁴ Indeed, the expectation that a manufacturer will obtain coverage, or self-insure through higher prices, for personal injury liability against third parties is one of the more widely accepted premises for the expansion of tort liability.

112. *West v. Caterpillar Tractor Co.*, 336 So. 2d 80, 86 (Fla. 1976); *Royal v. Black & Decker Mfg. Co.*, 205 So. 2d 307, 309 (Fla. 3d Dist. Ct. App. 1967), *cert. denied*, 211 So. 2d 214 (1968); RESTATEMENT (SECOND) OF TORTS § 402(A) cmt. g (1965); W. Page Keeton, *Products Liability—Liability Without Fault and the Requirement of a Defect*, 41 TEX. L. REV. 855, 858 (1963).

113. There is potential for unfairness. As one example of an obvious injustice, the effect might be to subject insurers to a new form of liability long after they negotiated their rates and the state approved them—an obvious injustice. See *Dimmitt Chevrolet, Inc. v. Southeastern Fidelity Ins. Corp.*, 636 So. 2d 700, 701-02 (Fla. 1993). See generally Owen, *supra* note 101, at 681 (demonstrating the inadequacy of the more general assumption that the expansion of tort liability can be based upon the availability of insurance).

114. If the seller of a product can buy a policy against personal injury liability, as Justice Blackmun asserts, it can insure against claims by the buyer of disappointed economic expectations. However, Brown and Feinman state insurance is not available for such a claim. Brown & Feinman, *supra* note 10, at 341. The difference may be explained by the fact that Justice Blackmun cites admiralty authorities for the availability of insurance: perhaps there are special maritime policies. That coverage is still common, even though expensive and it may be more prevalent than that against the costs attributable to the disappointed expectations of a buyer. Recent studies suggest 86% of the country's 500 largest corporations purchase some form of commercial casualty insurance. George L. Priest, *The Current Insurance Crisis in Modern Tort Law*, 96 YALE L.J. 1521, 1561 (1987).

Justice Blackmun was correct insofar as he spoke of a difference in degree. But scholars challenge the factual and logical conclusions he would draw from that distinction.¹¹⁵

As have so many others, Professor Priest deplores the high cost of tort litigation.¹¹⁶ He goes further, however, to question its practicality as a means to accomplish either insurance, compensatory, or regulatory functions.¹¹⁷

The traditional argument is that the availability of insurance justifies the expansion of tort liability. Priest's answer is that the expansion of tort

115. Some question the relative distribution power among the parties to the transaction, suggesting the buyer is in a better position to buy insurance against the loss because of the greater knowledge of the context in which the product must do the work. William K. Jones, *Product Defects Causing Commercial Loss: The Ascendancy of Contract Over Tort*, 44 U. MIAMI L. REV. 731, 765 (1990).

The standard casualty policy protects the buyer from losses associated with accidents caused by product failures, without segregation of risks or charges. The premium on such policies will be related to the value of the buyer's property and the general risk involved in the buyer's activities. These are matters about which the seller has limited knowledge and almost no control. As to such losses, the buyer is in the best position to obtain optimal coverage under its own policy, described as first party insurance. . . .

The avoidance of unnecessary transaction costs is a major advantage of having the buyer look to its own insurance company. Litigation over the liability of the seller can consume substantial resources, whether the suit is ultimately resolved in favor of the buyer or the seller.

. . . .
 . . . As to the consequences of the defect, the buyer exercises significant control, both in the manner in which the product is used and in precautions taken to avoid loss (such as periodic inspections and sensitivity to signs of trouble). In sum, the problem is one of joint care. In such cases, it is not possible to devise a liability rule that is optimal in all instances. For example, the diligence of the seller may be enhanced by increasing the probability that the seller will be held accountable for losses resulting from product defects. But the enhancement of seller diligence comes at the expense of buyer caution

Id. at 765-67 (footnote omitted).

116. Putting that concern in quantitative terms, he adds that the administrative costs of tort liability amounts to about 53% of the plaintiff's net recovery of benefits, whereas comparable insurance arrangements have an expense figure closer to 10%. Priest, *supra* note 114, at 1560.

117. *Id.* Priest also suggests that the burden of the change may fall disproportionately on the poor. *Id.* They receive less benefit through litigation since pain and suffering and disability payments are highly correlated with the individual's expected future income, while the insurance premium (ultimately incorporated in the price of the product) is set for the average loss. *Id.* at 1559. Conversely, the increases in prices which are necessary to accomplish the insurance function have a severe impact on them. *Id.* at 1525.

liability in fact makes insurance less available.¹¹⁸ The commentator goes

118. Professor Priest reminds us that deterrence is different from insurance and the two functions are not necessarily consistent. Priest, *supra* note 114, at 1525. In an oversimplified outline, his analysis is that it is not the simple increase in the amount of judgments which undermines the insurance market, but the tendency for expanded liability to undermine the advantages of the scale of the ability to predict the consequences and to apply the “law of large numbers” and for the tendency for higher premiums to drive low risk insureds to become self insurers, thus reducing the size of the pool of insureds and the cost for others. That process in turn feeds on itself as the fees grow higher, making it questionable whether the next level of insureds have a reason to stay with the carrier rather than become a self insurer. *Id.* at 1525-45. The central concept is the idea that the insurance defense depends upon the attendance of risks, and that the broadening of tort liability tends to eliminate the distinctions among risks, all are thrown together into a huge pool.

Consumers who systematically face a lower injury probability are likely to find the insurance provided with the product or service not worth its added premium. Many commentators have tended to view product-or service-related injuries as occurring randomly, generating an equal injury probability to each consumer. Many product-and service-related injuries, however, are systematically associated with particular product uses. Most modern products can be employed in a wide range of diverse activities. Those consumers who use products in typically less, rather than more, risky ways are likely to drop out of the consumer pool if tort law requires the manufacturer to insure all customer uses. These consumers will shift to alternative products or services that cannot be used in equally risky ways—products which, as a consequence, will be cheaper because of the lower attendant insurance premiums.

A familiar modern example is consumers use of four-wheel drive vehicles. In recent years, the liability of manufacturers of such vehicles has been expanded under design defect and warning law and, more generally, as courts have limited the defense of contributory negligence, misuse and assumption of risk. . . .

Manufacturers must respond to this increased liability either by changing product design to protect drivers in extreme conditions or by increasing insurance coverage for the consumer set as a whole. Whether the manufacturer changes the design or merely increases insurance coverage, product costs will increase and the product price will increase. The price increase, of course, may seem desirable for consumers who drive in extreme back road conditions. But consumers who purchase four-wheel drive vehicles for any other purposes . . . [for] driving on snowy or muddy roads—may not find the increased price worthwhile. These consumers could be lured away if they were offered a four-wheel drive vehicle suitable for snow and mud, but not for extreme grades which, if only because of the lower attendant insurance premium, could be offered at a lower price. It is not surprising that many manufacturers have begun offering van and station wagon models with a four-wheel drive option.

Id. at 1564-65 (footnotes omitted); see also Bruce Chapman & Michael Trebilock, *Punitive Damages: Divergence in Search of a Rationale*, 40 ALA. L. REV. 741, 778 (1989); Jones, *supra* note 115, at 731; Ernest J. Weinrib, *The Insurance Justification and Private Law*, 14

on to explain that insurance rates are set by predictions of future losses and that increased tort liability tends to force low-risk participants out of the insurance pool.¹¹⁹ This, in turn, drives up premiums across a broad range, making some activities too expensive to continue.¹²⁰ He suggests, as well, that the comparative advantage which insurance companies have in the aggregation of risks—one of the theoretical foundations of the industry—is overwhelmed by the coverage obligations which tort law inflicts upon them as well as the concomitant reduction in their ability to segregate risks.

J. LEGAL STUD. 681 (1985).

119.

This process is adverse selection in the product market. . . . Because the manufacturer was prohibited by product liability law from making this additional insurance optional, low-risk consumers within the pool—those not intending to expose themselves to backcountry risks—dropped out of the pool, either by shifting to domestic four-wheels, or by declining to buy the product at all. When low risk consumers drop out, the insurance premiums added to the price of backcountry four-wheels must be increased by an ever greater amount.

The second set of low-risk consumers affected by the expansion of provider liability are the low-income or poor, who bring low risk to a liability insurance pool because of the lower damages they will receive because of their lower income and poorer future employment prospects. As the insurance premiums tied to products and services increase, these consumers also drop out because the price they must pay is increasingly greater than the value received. Such consumers will shift to substitute products . . . Again, as this set of low-risk consumers drops out, the attendant insurance premiums must be commensurately increased.

Adverse selection and consumer risk . . . also provides the only explanation of why increases in corporate tort liability compel providers to withdraw products and services from markets altogether. Again, if there were no adverse selection, increases in insurance premiums or self-insurance costs could largely be passed on to consumers. Sales may decline, as must be expected from any price increase, but there would be no reason to withdraw products from the market. There is a different effect, however, where a price increase derives from increasing risk pool variance. Increasing variance generates adverse selection by low-risk consumers who successively drop out of the pool. The pool, as a consequence, unravels. At some point, demand for the product sold with the necessary insurance premium simply disappears. There remains no set of identifiable consumers to whom the product or service is worth its price.

. . . The large number of products and services that have been totally withdrawn from markets demonstrate the severity of the effects of contemporary tort law's shift to the third-party insurance mechanism.

Priest, *supra* note 114, at 1565-67.

120. *Id.* at 1569-70 (providing asbestos production as an example).

XIII. CONCLUSION

Product liability law rests on the moral perception that the economic burdens of death or incapacitation are too much for an individual. But in *Santor v. A & M Karagheusian, Inc.*,¹²¹ that exception transformed itself into a norm for commercial transactions in which no one is injured. Disturbing in itself, the metamorphosis illustrates a recurring paradox.

The field traditionally is thought to be governed by a sense of practical justice which cuts through technical limitations and restraints. Yet as a new principle gains acceptance, advocates shove practical difficulties to the background and urge the courts to carry the approach to extremes in deference to its theoretical basis.¹²²

At least in the instance of the economic loss rule, that reasoning has grown conclusory and even circular. Ignoring the need for empirical evidence of social need and effect, courts too often react automatically to slogans of past product liability battles.

To the unfriendly eye, this is little better than the Mandarin theorizing which led Traynor and other reformers to take up arms decades ago. Over-used, the Marseillaise has decayed into Muzak.

121. 207 A.2d 305 (N.J. 1965).

122. See Dorsey D. Ellis, Jr., *Punitive Damages, Due Process and the Jury*, 40 ALA. L. REV. 975 (1989).