Architects' Liability to Third Party Contractors for Economic Loss Resulting from Faulty Plans and Specifications

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An architect's or builder's liability for the faulty design or construction of a building has undergone major changes over the years. Under the Code of Hammurabi, if a builder's careless construction of a house resulted in the death of the owner's son, the builder's son would be put to death.[1] Although the remedy was less harsh, the liability was no less strict under the Code Napolean, which provided that an architect was responsible for ten years for the partial or entire "perishing" of a building, even if such loss resulted from poor soil.[2]

Whether due to moral enlightenment[3] or historical accident,[4] tort liability gradually became associated more with fault than with strict liability. This trend away from strict tort liability, which had achieved a rather full development by the end of the nineteenth century,[5] went to an extreme in the case of architects. By the late nineteenth century, English courts had replaced architects' strict liability with a broad immunity.[6]

Under the English immunity rule, an architect was a quasi-arbitrator between the contractor and the owner and was liable for fraud or collusion but not for negligence.[7] Early American courts adopted this rule,[8] some even holding architects immune to allegations of fraud or corruption.[9] Arizona courts applied the immunity rule until fairly recently.[10]

Courts have narrowed the broad protection once afforded architects in various ways. This Note focuses on the broadening of architects' liability for economic loss suffered by third party contractors relying on negligently prepared plans and specifications. Potentially applicable theories of liability are

1. Witherspoon, *Architects' and Engineers' Tort Liability*, 16 DEFENSE L.J. 409 (1967).
2. CODE NAPOLEAN art. 1792.
3. W. PROSSER, THE HANDBOOK OF THE LAW OF TORTS 492 (4th ed. 1971).
4. D. B. DOBBS, TORTS AND COMPENSATION: PERSONAL ACCOUNTABILITY AND SOCIAL RESPONSIBILITY FOR INJURY 493-518 (1985).
5. *See* W. PROSSER, *supra* note 3, at 492.
6. Witherspoon, *supra* note 1, at 409-10.
7. *Id.* at 409.
8. *Id.* at 410.
9. Wilder v. Crook, 250 Ala. 424, 34 So. 2d 832 (1948), *cited in* J. ACRET, ARCHITECTS AND ENGINEERS: THEIR PROFESSIONAL RESPONSIBILITIES § 10.9, at 177 (1977).
10. *See infra* text accompanying notes 31 through 34.

considered. This Note then addresses the central issue of whether negligence liability should be based upon reasonable foreseeability or upon the narrower standard of negligent misrepresentation.

THE THEORIES OF LIABILITY

Courts addressing architects' liability to third party contractors for economic loss resulting from negligently prepared plans have considered four general theories of liability: (1) third party beneficiary liability; (2) breach of implied warranty; (3) strict liability in tort; and (4) negligence. Architects' liability is severely limited under the third party beneficiary theory and generally unavailable under implied warranty and strict liability theories.

Third Party Beneficiary Liability

The fact pattern which this Note addresses is one where there is no contractual privity between the architect and the contractor; the only contractual relationships are between the owner and the architect and between the owner and the contractor. Consequently, the contractor might claim to be a third party beneficiary of the owner-architect contract. Courts generally hold that the contracting parties must intend to benefit an individual before that individual can recover as a third party beneficiary.[11] Moreover, courts sometimes hold that the contract itself must show a clear intention to benefit the person claiming damages under the contract.[12] Courts have thus held that design professionals, such as architects and engineers, are not liable to third party contractors where the contract language does not express that their duties are intended to benefit the contractors.[13] One court expressed this general rule as creating a presumption that the contractor is an *incidental* beneficiary, as opposed to an *intended* beneficiary, unless the owner-architect contract manifests a clear intention to the contrary.[14]

Breach of Implied Warranty

The general rule is that a person dissatisfied with architectural services has no action against the architect for breach of implied warranty.[15] Moreover, courts have held that the implied warranties in the Uniform Commercial Code are inapplicable in such cases because a contract for architectural services is not a contract for the sale of goods.[16] Courts have also held that

11. J. MURRAY, MURRAY ON CONTRACTS § 279 (2d ed. 1974).

12. *See, e.g.*, Norton v. First Federal Sav., 128 Ariz. 176, 178, 624 P.2d 854 (1981); Stewart v. Arrington Const. Co., 92 Idaho 526, 446 P.2d 895 (1968).

13. *See, e.g.*, Harbor Mechanical, Inc. v. Arizona Elec. Power Coop., Inc., 496 F. Supp. 681, 684 (D. Ariz. 1980); A.R. Moyer, Inc. v. Graham, 285 So. 2d 397 (Fla. 1973).

14. A.R. Moyer, Inc. v. Graham, 285 So. 2d 397, 403 (Fla. 1973).

15. *See, e.g.*, City of Mounds View v. Walijarvi, 263 N.W.2d 420 (Minn. 1978); Board of Trustees of Union College v. Kennerly, 167 N.J. Super. 311, 400 A.2d 850 (1979); Sears, Roebuck & Co. v. Enco Assoc., Inc., 42 N.Y.2d 389, 398, 401 N.Y.S.2d 767, 772, 372 N.E.2d 555, 559 (1977). This rule was expressed as long ago as 1898. Chapel v. Clark, 117 Mich. 638, 640, 76 N.W. 62 (1898), *cited in* Borman's, Inc. v. Lake State Dev. Co., 60 Mich. App. 175, 182, 230 N.W.2d 363, 370 (1975).

16. Rosos Litho Supply Corp. v. Hansen, 123 Ill. App. 3d 290, 462 N.E.2d 566 (1984) (action by third party contractor against architect); Queensbury Union Free School Dist. v. Jim Walter Corp., 91 Misc. 2d 804, 806, 398 N.Y.S.2d 832 (1977).

no other type of statutory or implied common law warranty is applicable to architectural services.[17]

The Arizona Supreme Court recognizes the general rule that design professionals do not impliedly warrant the accuracy of their work.[18] Nonetheless, the court recently held that a lower court erred in dismissing a third party contractor's claim for breach of implied warranty against architects for negligently prepared plans.[19] Although the court merely held that the trial court was mistaken in imposing a privity requirement on a claim for breach of common law warranty, the holding suggests that the contractor had stated a cause of action for breach of implied warranty.[20]

Strict Liability

One obstacle to applying strict tort liability to cases in which third party contractors sue architects for economic loss is courts' refusal to impose strict liability for purely economic loss.[21] Beyond that, however, courts consistently refuse to apply strict liability to architects regardless of the type of loss involved.[22] The reasons for courts' refusal include the following: strict liability is not imposed on one who merely provides services;[23] architects are not sufficiently analogous to manufacturers or distributors who place goods in the stream of commerce;[24] a cause of action for strict liability is only possible where there is also a cause of action for implied warranty;[25] architectural sciences are too imprecise.[26] When the Arizona Court of Appeals faced the issue, it refused to address the applicability of strict liability to architectural plans on the ground that no evidence was presented showing any defect in the plans.[27]

Negligence Liability

Architects' negligence liability, historically quite limited, has expanded in recent years. It offers the most promising theory for recovery against

17. *Rosos*, 462 N.E.2d at 571.

18. Donnelly Constr. Co. v. Oberg/Hunt/Gilleland, 139 Ariz. 184, 189, 677 P.2d 1292, 1297 (1984).

19. *Id.*

20. The curious nature of this implied warranty is suggested by the court's claim that design professionals "warrant merely that they have exercised their skills with care and diligence and in a reasonable, non-negligent manner." *Id.*

21. *See, e.g.*, Fredonia Broadcasting Corp. v. RCA Corp., 481 F.2d 781 (5th Cir. 1973) (applying Texas law); Beauchamp v. Wilson, 21 Ariz. App. 14, 515 P.2d 41 (1973); Local Joint Executive Bd. of Las Vegas, Culinary Workers Union v. Stern, 98 Nev. 409, 651 P.2d 637 (1982). There have been occasional exceptions to this general rule. W. PROSSER, *supra* note 5, at 708 n.4. Those exceptions, however, have been criticized. *Id.* at 708.

22. Van Ornum v. Otter Tail Power Co., 210 N.W.2d 188 (N.D. 1973); *see generally* cases cited *infra* notes 23-26.

23. Del Mar Beach Club v. Imperial Contracting Co., 123 Cal. App. 3d 898, 176 Cal. Rptr. 886 (1981); *see generally* Annot., 29 ALR 3d 1425 (1968).

24. K-Mart Corp. v. Midcon Realty Group of Conn., 489 F. Supp. 813, 819 (D. Conn. 1980) (applying Connecticut law); Stuart Crestview Mutual Water Co., 34 Cal. App. 3d 802, 811, 110 Cal. Rptr. 543, 549 (1973).

25. Queensbury Union Free School Dist. v. Jim Walter Corp., 91 Misc. 2d at 807-08, 398 N.Y.S.2d at 836.

26. City of Mounds View v. Walijarvi, 263 N.W.2d 420, 424 (Minn. 1978).

27. Reber v. Chandler High School Dist. No. 202, 13 Ariz. App. 133, 474 P.2d 852 (1970).

architects whose faulty plans and specifications cause economic injury to third party contractors.

The Arizona Supreme Court narrowed the broad immunity enjoyed by architects in *Craviolini v. Scholer & Fuller Associated Architects*.[28] In *Craviolini*, a contractor sued for economic losses, alleging that the architects prepared defective plans and specifications. The trial court granted the architects' motion to dismiss on the ground that architects were immune as arbitrators or quasi-arbitrators.[29] In reversing, the Arizona Supreme Court held that an architect assumes many roles and enjoys immunity only when acting as an arbitrator.[30] Since the tortious acts were not connected with the adjudication of a dispute, the court held that the architects enjoyed no special immunity.[31] *Craviolini* is part of a modern trend expanding architects' negligence liability.[32] *Craviolini* expanded that liability in Arizona by limiting the immunity architects enjoyed under the English rule.[33]

Courts have further expanded architects' negligence liability by abolishing the privity defense in cases where a contractor suffers economic harm by relying on an architect's negligently prepared plans or specifications.[34] The rule that a contracting party is not liable in tort to a third party with whom the contracting party is not in privity of contract is traceable to the English case of *Winterbottom v. Wright*.[35] The privity rule's justification is based on

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28. 89 Ariz. 24, 357 P.2d 611 (1960).

29. *Id.* at 27, 357 P.2d at 613.

30. *Id.* at 28, 357 P.2d at 614.

31. *Id.*

32. Witherspoon, *supra* note 1, at 410. *See also* J. SWEET, LEGAL ASPECTS OF ARCHITECTURE, ENGINEERING AND THE CONSTRUCTION PROCESS 830-31, 866-67 (2d ed. 1977).

33. Vestiges of the broader English immunity can still be seen in the Arizona Revised Statutes. J. ACRET, *supra* note 9, at 225 states: "The courts in Arizona have abrogated the judicial doctrine of sovereign immunity. Yet ARIZ. REV. STAT. ANN. § 45-715 provides that no action shall be brought against the state, the state engineer or any employee of the state for damages sustained through the partial or total failure of any dam." Although ARIZ. REV. STAT. ANN. § 45-715 protects the state *engineer* from liability for failure of a dam, it is common to treat architects' and engineers' liability together. *See, e.g.*, J. ACRET, *supra*; Witherspoon, *supra* note 1, at 410-11; J. SWEET, *supra* note 32.

34. E.C. Ernst, Inc. v. Manhattan Constr. Co. of Texas, 551 F.2d 1026 (5th Cir. 1977), *cert. denied*, 434 U.S. 1067 (1978); Detweiler Bros., Inc. v. John Graham & Co., 412 F. Supp. 416 (E.D. Wash. 1976); Donnelly Constr. Co. v. Oberg/Hunt/Gilleland, 139 Ariz. 190, 677 P.2d 1298 (Ct. App. 1984); A.R. Moyer, Inc. v. Graham, 285 So. 2d 397 (Fla. 1973). At least one jurisdiction, however, retains the privity defense in suits against design professionals for economic loss. Peyronnin Constr. Co. v. Weiss, 137 Ind. App. 417, 208 N.E.2d 489 (1965). *See also* Barnes v. Hampton, 198 Neb. 151, 252 N.W.2d 138 (1977) (contractor's assignee barred from bringing action against subcontractor subsequent to settlement of contractor's action against the owner).

It is sometimes said that design professionals are subject to the "professional standard" of care. W. PROSSER, *supra* note 3, at 150; City of Eveleth v. Ruble, 302 Minn. 249, 250, 225 N.W.2d 521, 522 (1974) (design professional is under a duty "to exercise such care, skill, and diligence as men in that profession ordinarily exercise under like circumstances."). Courts, however, tend to simply apply a reasonable foreseeability test in the context of determining design professional's liability to third party contractors for economic loss resulting from defective plans and specifications. *Donnelly*, 139 Ariz. at 187-77, 677 P.2d at 1295-96; A.R. Moyer, Inc. v. Graham, 285 So. 2d 397, 402 (Fla. 1973); A.E. Investment Corp. v. Link Builders, Inc., 62 Wis. 2d 479, 214 N.W.2d 764, 767 (1974). Two jurisdictions regard foreseeability as one of several factors to be considered in determining an architect's negligence liability to third party contractors for economic loss. United States v. Rogers and Rogers, 161 F. Supp. 132 (S.D. Cal. 1958); Conforti & Eisele, Inc. v. John C. Morris Assocs., 175 N.J. Super. 341, 343, 418 A.2d 1290, 1292 (1980). Accordingly, "negligence liability" of architects to third party contractors is treated in this Note as resting on reasonable foreseeability, rather than the standard of care exercised by some community of architects.

35. 10 M. & W. 109, 152 Eng. Rep. 402 (1842). In *Winterbottom*, the driver of a mail coach

a concern with limiting a defendant's liability by limiting the class of persons to whom he is liable.[36]

Winterbottom simply limited a party's contractual liability to those with whom he is in privity of contract.[37] Courts subsequently interpreted the case as also limiting a party's tort liability to those with whom he is in privity of contract.[38] Exceptions to this broad privity rule, however, soon developed. In 1852, just ten years after *Winterbottom*, a New York court held a seller liable in negligence for the sale of an "inherently dangerous" article even though the seller and buyer were not in privity of contract.[39] In 1916, Justice Cardozo, in *MacPherson v. Buick Motor Co.*,[40] extended the class of inherently dangerous items to include any article which would be unsafe if not carefully made. *MacPherson* caused the exception to swallow the rule and is now law in every state.[41]

Courts have been slower to abandon the privity rule where economic rather than physical harm is suffered[42] and where services rather than sales are the object of the contracts.[43] Arizona courts have been no exception.[44]

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was injured when the coach collapsed on him. The defendant was under a contractual duty to keep the coach in repair. The plaintiff sued on the theory that the defendant had breached his contractual duty to maintain the coach. The court held that the plaintiff could not maintain a cause of action on the contract. *Id.* at 114-16, 152 Eng. Rep. at 404-05. Subsequent courts, however, misinterpreted *Winterbottom* to mean that in the absence of privity of contract, a third party could not maintain an action in tort against anyone who improperly performed his contractual duties. W. PROSSER, *supra* note 3, at 522, 641. That the privity rule actually resulted from a misinterpretation of *Winterbottom* was apparently not revealed in print until 1905. *Id.* at 641. By that time the privity rule was well entrenched. *Id.* See also 2 F.V. HARPER & F. JAMES, THE LAW OF TORTS § 18.5, at 1040 (1956). For a discussion of the holding in *Winterbottom* see Bohlem, *The Basis of Affirmative Obligations in the Law of Torts*, 53 AM. L. REG. 209, 281-85 (1905).

36. Lord Abinger expressed his concern, in dictum:

> [I]f the plaintiff can sue, every passenger, or even any person passing along the road, who was injured by the upsetting of the coach, might bring a similar action. Unless we confine the operation of such contracts as this to the parties . . . . the most absurb and outrageous consequences, to which I can see no limit, would ensue.

Winterbottom, 10 M. & W. at 114, 153 Eng. Rep. at 405.

37. Bohlen, *supra* note 35, at 281-85.

38. The limitation actually intended by *Winterbottom* is a sound one. It has been pointed out with respect to tort liability that the scope of liability should be limited by the basis of that liability. R.E. KEETON, LEGAL CAUSE IN THE LAW OF TORTS, 18-19 (1963). This is, of course, really an expression of the rule of Palsgraf v. Long Island R.R., 248 N.Y. 339, 162 N.E. 99 (Ct. App. 1928). Although Keeton was discussing liability for negligence, the *Palsgraf* insight is equally appliable to contractual liability. According to the popular misinterpretation of *Winterbottom*, however, the court was limiting a person's liability *in tort* to those with whom he is in privity of contract. This privity rule, which would limit the scope of tort liability by the basis of contract liability, has been justifiably criticized. Bohlem, *Fifty Years of Torts*, 50 HARV. L. REV. 1225, 1232-34 (1937); W. PROSSER, *supra* note 3, at 622.

39. Thomas v. Winchester, 6 N.Y. 397 (1852). For a discussion of the development outlined in the text accompanying notes 39-41 see W. PROSSER, *supra* note 35, at 1041-42.

40. 217 N.Y. 382, 111 N.E. 1050 (1916).

41. W. PROSSER, *supra* note 3, at 643.

42. Prosser, *Misrepresentation and Third Persons*, 19 VAND. L. REV. 231 (1966).

43. W. PROSSER, *supra* note 3, at 622-23.

44. Arizona courts have preserved the privity defense where a buyer seeks to recover economic loss from a manufacturer in products liability actions for breach of implied warranty of merchantability. Flory v. Silvercrest Ind., Inc., 129 Ariz. 574, 633 P.2d 383 (1981). *See* Comment, *Products Liability: Privity Requirement for Recovery of Economic Loss Withstands Assault*, 23 ARIZ. L. REV. 524 (1981). The reluctance of Arizona courts to abandon the privity defense where services rather than sales are the object of the contract appears in the context of attorneys' liability. Chalpin v. Brennan, 114 Ariz. 124, 126, 559 P.2d 680, 682 (Ct. App. 1976). For a discussion of *Chalpin* and

Consequently, an architect's liability for economic loss suffered by contractors who rely on negligently prepared plans and specifications falls within the privity rule's strongest area of protection. That architects would eventually lose this protection, however, was almost inevitable given the erosion of the privity defense[45] and the expansion of architects' liability.[46]

THE PRIVITY RULE IN ARIZONA AND ARCHITECTS' NEGLIGENCE LIABILITY FOR ECONOMIC LOSS

Arizona first addressed architects' liability to third parties for economic loss arising from defective plans and specifications in *Blecick v. School District No. 18 of Cochise County*.[47] In *Blecick*,[48] construction contractors sued to recover an amount claimed due under a construction contract between the contractors and a school district. The contractors sued both the school district and the architects who had been hired by the school board. The contractors alleged that defects in the completed construction were due solely to the architects' defective plans and specifications. The court of appeals framed the issue vaguely.[49] The court stressed the lack of privity between the contractors and the architects and held that the contractors had no cause of action.[50] Although the Arizona Court of Appeals later pointed out the unclear nature of the contractors' cause of action in *Blecick*, it concluded that *Blecick's* privity requirement "appears" to apply to tort as well as to contract actions.[51] At least one other court has adopted this interpretation of *Blecick's* holding.[52]

The uncertainty surrounding whether the *Blecick* holding simply bars actions by contractors against third party architects in contract or whether it also bars actions in negligence is strikingly reminiscent of the confusion surrounding *Winterbotton v. Wright*. The general view that *Blecick*, like the popular misinterpretation of *Winterbotton*, bars tort action enhances the similarity. A major dissimilarity between *Blecick* and *Winterbottom*, however, is marked by the different rules of pleading in force at the times of the two cases. To properly understand *Winterbotton*, one must keep in mind the rigidity of the pleading rules employed by the Court of Exchequer at the time and the fact that the only breach alleged by the plaintiff was a breach of

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a criticism of the privity defense applied therein see Comment, *Attorney Liability to Third Parties*, 19 ARIZ. L. REV. 653 (1977).

45. *See supra* notes 39-41.

46. *See supra* note 35.

47. 2 Ariz. App. 115, 406 P.2d 750 (1965), *overruled by* Donnelly Constr. Co. v. Oberg/Hunt/Gilleland, 139 Ariz. 184, 677 P.2d 1292 (1984).

48. The facts of *Blecick* are set out 2 Ariz. App. at 118, 406 P.2d at 753.

49. The court stated the issue as follows: "Is an architect liable to a contractor for the preparation of defective plans and specifications?" *Id.* at 119, 406 P.2d at 754. As the issue is framed, it is unclear whether a negative answer would mean that an architect is not liable on the contract or whether an architect is not liable at all to a contractor for the preparation of defective plans and specifications.

50. The court held that "[t]he mere coexistence of the two contracts, with one contracting party (the School District) common to both, does not give the plaintiffs a right to enforce obligations owed by the architects to the School District." *Id.* at 120, 406 P.2d at 755.

51. *Donnelly*, 139 Ariz. at 192, 677 P.2d at 1300.

52. Harbor Mechanical, Inc. v. Arizona Elec. Power Coop., Inc., 496 F. Supp. 681, 683 (D. Ariz., 1980).

defendant's contractual duty to keep the coach in repair.[53] Thus, while *Blecick* and *Winterbottom* are similar on their holdings and in the particular vagueness of their opinions, the liberality of modern pleading rules legitimizes a broad interpretation of the *Blecick* holding. That the Arizona court could have easily viewed the contractors' complaint as stating a cause of action in negligence and that the court expressed its finding in very broad language both support the view that *Blecick* bars negligence actions by contractors against third party architects for defective plans and specifications.

Harbor Mechanical, Inc. v. Arizona Electric Power Cooperative, Inc.[54] was the first case to analyze the *Blecick* decision. In *Harbor Mechanical*, two contractors sued engineers for the economic loss allegedly suffered as a result of the engineers' negligently prepared plans and specifications and negligent supervision. The U.S. District Court of Arizona held that *Blecick* required a finding in the engineers' favor.[55] The court viewed *Blecick* as prohibiting the contractors' recovery for negligence absent privity between the architect and the contractor.[56]

Donnelly Construction Co. v. Oberg/Hunt/Gilleland[57] was the first Arizona case to present a direct challenge to the validity of the *Blecick* privity

53. Bohlen, *supra* note 35, at 281-82.

54. 496 F. Supp. 681 (D. Ariz. 1980).

55. *Id.* at 683-84.

56. *Id.* at 683. The engineers attempted to distinguish *Blecick* by arguing that the action in *Blecick* was on the contract while in *Harbor Mechanical* the action was negligence. The court rejected this distinction on the ground that the contractors' negligence count "substantially premises the defendants' alleged duty to plaintiffs on the contract between [the engineers] and AEPCO." *Id.* This is rather odd. To insist on viewing the contractors' negligence claim, denominated as such, as one founded in contract does not really seem in the spirit of modern pleading rules. Although the contractors' position was that the duty breached by the engineers arose from the contract, the contractors alleged sufficient facts to support a prima facie case of negligence based on foreseeability. Moreover, having chosen to interpret *Blecick* as barring actions in negligence by contractors against architects with whom there was lack of privity, it would have been natural for the court to respond to the contractors' move by saying that they had misinterpreted *Blecick*. The court could then have agreed that the contractors' cause of action was based in negligence and thus barred by *Blecick*.

The court rejected the contractors' position that Reber v. Chandler High School Dist. No. 202, 13 Ariz. App. 133, 474 P.2d 852 (1970), had implicitly overruled *Blecick*. *Id.* In *Reber*, a school district entered a contract with an architect under which the architect was to prepare plans and specifications and supervise the construction of a physical education building. The roof of the partially completed structure collapsed, injuring employees of the general contractor. Those employees sued both the school district and the architect under theories of strict liability for defective plans and negligent supervision by the architect. The court declined to address the strict liability doctrine's applicability on the ground that no evidence was presented showing any defect in the plans and specifications. The court focused on the plaintiffs' contention that the school district had retained certain supervisory powers and had vested these in the architect who in turn negligently exercised them. The court held that liability could only attach in such a case when a duty arises from the reservation of the right to exercise daily control over the work.

Thus, the *Reber* court recognized that an architect could be liable to the employees of the general contractor for negligent supervision. The plaintiffs in *Harbor Mechanical* argued that *Reber* thus implicitly overruled *Blecick*. *Id.*

The court rejected this contention, observing that the *Reber* court looked to the contract language to determine whether the parties intended that the architect would exercise the detailed supervisory control alleged by the plaintiffs. *Id. Reber* was thus viewed as consistent with *Blecick* in that both "would confine the duties imposed upon an architect to those contemplated by the contract." *Id.* at 684. Another way to reconcile *Reber* and *Blecick* is to note that *Reber* is a personal injury case while *Blecick* is an economic loss case. *See supra* text accompanying note 42.

57. 139 Ariz. 190, 677 P.2d 1298 (Ct. App. 1983), *vacated*, 139 Ariz. 184, 677 P.2d 1292 (1984).

rule. In *Donnelly*,[58] a school district employed architects to prepare plans and specifications for a construction project. Donnelly Construction Company sued the school district and the architects alleging that those plans and specifications were defective. The architects filed a motion to dismiss for failure to state a claim against them. They asserted that since there was no privity of contract between the architects and Donnelly, the architects owed no duty to Donnelly. The trial court granted the architects' motion. On appeal, the Arizona Court of Appeals held that the *Blecick* privity rule and the *Craviolini* expanded liability rule were not contrary; thus *Craviolini* did not require that *Blecick* be rejected.[59] The court, however, criticized the privity rule for its failure to recognize the different bases of liability in tort and contract. The court reasoned that because these bases of liability differ, those who may seek enforcement under the two theories will also differ. While it is privity which determines who may enforce contractual liability, it is foreseeability which determines who may enforce tort liability.[60] The court thus found no conceptual problem with the possibility that a contracting party might owe a duty in tort to some non-contracting third party by virtue of that contracting party's entering into the contract.[61] The court concluded that if *Blecick* is inconsistent with this result, it must be rejected. Having concluded that lack of privity does not bar architects' liability to third party contractors for faulty plans and specifications, the court considered the problem of avoiding the potentially unlimited liability contemplated in *Winterbottom*.[62] The court adopted Restatement (Second) of Torts § 552 as the proper solution.[63]

RESTATEMENT SECTION 552: NEGLIGENT MISREPRESENTATION

Under negligent misrepresentation, one who negligently obtains or communicates information can be liable for pecuniary loss suffered by those

58. The facts in *Donnelly* are set out 139 Ariz. at 191, 677 P.2d at 1299.

59. *Donnelly*, 139 Ariz. at 193, 677 P.2d at 1301. The court pointed out that in *Craviolini*, the tortious conduct was unrelated to the duties arising out of the architect-owner contract. In *Blecick*, however, the source of liability would have been the architect's "negligent performance of its contractual obligations." *Id.* The court concluded that *Blecick* and *Craviolini* were not contrary. *Id.*

60. *Id.* at 194, 677 P.2d at 1302.

61. *Id.*

62. *See supra* note 36 and accompanying text.

63. RESTATEMENT (SECOND) OF TORTS § 552 (1977) provides:

§ 552. Information Negligently Supplied for the Guidance of others

(1) One who, in the course of his business, profession or employment, or in any other transaction in which he has a pecuniary interest, supplies false information for the guidance of others in their business transactions, is subject to liability for pecuniary loss caused to them by their justifiable reliance upon the information, if he fails to exercise reasonable care or competence in obtaining or communicating the information.

(2) Except as stated in Subsection (3), the liability stated in Subsection (1) is limited to loss suffered

(a) by the person or one of a limited group of persons for whose benefit and guidance he intends to supply the information or he knows that the recipient intends to supply it, and

(b) through reliance upon it in a transaction that he intends the information to influence or knows that the recipient so intends or in a substantially similar transaction.

(3) The liability of one who is under a public duty to give the information extends to loss suffered by any of the class of persons for whose benefit the duty is created, in any of the transactions in which it is intended to protect them.

who rely on the information, notwithstanding lack of privity of contract.[64] The liability imposed for negligent misrepresentation is narrower than ordinary negligence liability based upon reasonable foreseeability. To be liable under negligent misrepresentation, the defendant must have a pecuniary interest in supplying the information.[65] Moreover, the defendant is only liable to a person or to one of a limited class of persons "for whose benefit and guidance he intends to supply it."[66] Finally, the defendant's liability to such persons is limited to those losses incurred in transactions which the defendant intends the information to influence or in transactions of a kind which the defendant knows that the recipient so intends.[67] In negligence cases, the class of persons protected and the class of harm protected against are ordinarily delimited by the reasonable foreseeability test.[68] Negligent misrepresentation, however, bases liability on the defendant's knowledge or intention,[69] thus restricting both the class of persons protected and the class of harm protected against.

In *Donnelly*, the question was whether the plaintiff contractor and its loss fell within the narrower scope of protection afforded by negligent misrepresentation. The court of appeals did not answer this question but remanded, holding that if the plaintiff could establish liability under section 552, lack of privity would not bar the architects' liability.[70] The opinion, however, does reveal how narrowly the court intended to construe liability for negligent misrepresentation. In dictum, the court discussed *Phoenix Title and Trust Co. v. Continental Oil Co.*,[71] and indicated that defendants are liable for negligent misrepresentation only if they had *actual knowledge* of both the particular purpose for which the information would be made available and the fact that it would be made available to particular persons.[72]

In *Phoenix Title*,[73] a buyer of realty relied to his detriment on a negligently prepared abstract of title. The court held that the abstractor was not liable to the purchaser because of a lack of privity. In viewing *Phoenix Title* as consistent with the adoption of section 552, the court of appeals in *Donnelly* stated that the abstractor in *Phoenix Title* did not know the specific purpose to which the abstract would be put.[74] There are, however, relatively few purposes to which abstracts of title are generally put. Despite the extremely high probability that an abstract of title will be used to give a buyer the "green light" to go ahead with a purchase, the court of appeals apparently wanted something more precise before imposing liability.

The *Donnelly* court also pointed out that the abstractor in *Phoenix Title* did not know that the abstract would be provided to any particular person or

64. RESTATEMENT (SECOND) OF TORTS § 552 comment h (1977).
65. *Id.* subsection (1).
66. *Id.*, subsection 2(a).
67. *Id.*, subsection 2(b).
68. Palsgraf v. Long Island R.R. Co., 248 N.Y. 339, 162 N.E.2d (1928).
69. *See supra* notes 66 and 67 and accompanying text.
70. *Donnelly*, 139 Ariz. at 195, 677 P.2d at 1303.
71. 43 Ariz. 219, 29 P.2d 1065 (1934).
72. *Donnelly*, 139 Ariz. at 196, 677 P.2d at 1304.
73. The facts of *Phoenix Title* are set out 43 Ariz. at 221-26, 29 P.2d at 1065-68.
74. *Donnelly*, 139 Ariz. at 196, 677 P.2d at 1304.

group of persons.[75] Since, however, there will be a rather limited group of potential buyers of a particular piece of realty in a particular neighborhood at a particular time and at the particular selling price, the group of persons who might foreseeably rely on a given abstract of title is limited. This limitation was apparently not sufficient under the *Donnelly* dictum.

The implication of the court of appeals discussion of *Phoenix Title* is that the architects would be liable to Donnelly only if they had *actual knowledge* that the plans would be made available to particular persons for the specific purpose of calculating and submitting bids. This is the result despite the probability that the architects are substantially certain that contractors use the plans in submitting bids. Conversely, if the court applied ordinary negligence as the theory of liability, Donnelly's position as a bidding contractor and the reasonable foreseeability that bidding contractors would use the plans would mandate the architects' liability.[76]

Two issues remained after the court of appeals *Donnelly* opinion: (1) whether architects are liable to third party contractors for economic loss caused by negligently prepared plans only where the narrower negligent misrepresentation standard is met, or whether negligence based on reasonable foreseeability applies, and (2) whether the standard of liability for negligent misrepresentation is as narrow as the *Donnelly* appeals decision indicates.

Regarding the second issue, the Restatement indicates that a defendant acts with the intent to bring about a result if the defendant is substantially certain that the result will occur.[77] Reading together the Restatements' definition of "intent" and its analysis of negligent misrepresentation makes clear that if an architect is substantially certain that bidding contractors will be guided by his plans in submitting bids, the architect can be liable to those contractors for negligent misrepresentation. Liability under negligent misrepresentation is thus not as narrow as the *Donnelly* dictum regarding *Phoenix Title* indicated.[78] If the court of appeals intended that negligent misrepresentation govern architects' liability to third parties for economic loss resulting from negligently prepared plans, then it could not offer *Phoenix Title* as guidance for its holding. Conversely, if the court of appeals intended *Phoenix Title* to offer guidance, it could not have intended that negligent misrepresentation govern the problem. The *Donnelly* dictum regarding *Phoenix Title* thus created an uncertainty for Arizona courts regarding the scope of liability for negligent misrepresentation. A court could only resolve this uncertainty by rejecting *Phoenix Title* or by rejecting or modifying the negligent misrepresentation doctrine.

The Arizona Supreme Court resolved this issue. In the *Donnelly* appeal to the Arizona Supreme Court,[79] the court disapproved of *Phoenix Ti-*

75. *Id.*

76. *See supra* note 68 and accompanying text.

77. RESTATEMENT (SECOND) OF TORTS § 8A. "Intent: The word "intent" is used throughout the Restatement of this subject to denote that the actor desires to cause consequences of his act, or that he believes that the consequences are substantially certain to result from it." *See also*, Garratt v. Dailey, 46 Wash. 2d 197, 279 P.2d 1091 (1955).

78. *See supra* notes 71 and 75 and accompanying text.

79. Donnelly Constr. Co. v. Oberg/Hunt/Gilleland, 139 Ariz. 184, 677 P.2d 1292 (1984).

tle[80] and expressly held that the *Donnelly* contractor had stated a cause of action in negligent misrepresentation against the architects. The supreme court cleared up the confusion and inconsistentcy raised by the appeals court by holding that the negligent misrepresentation doctrine, unhampered by *Phoenix Title*, applies to suits by contractors against architects for defective plans.[81]

NEGLIGENCE VS. NEGLIGENT MISREPRESENTATION

The question remaining after the *Donnelly* court of appeals opinion, whether architects are liable only under a negligent misrepresentation theory or whether liability can also be based on an ordinary negligence theory, was resolved by the Arizona Supreme Court in its *Donnelly* opinion. The court confirmed the court of appeals' holding that *Blecick* is overruled to the extent that it holds that lack of privity precludes an action in tort by a contractor against an architect for negligently preparing plans and specifications.[82] Moreover, the Arizona Supreme Court went beyond the court of appeals' premise that privity is no defense and concluded that the contractor had stated a cause of action in negligence under the reasonable foreseeability test.[83] Thus, architects lost any special protection under the narrower liability rule for negligent misrepresentation. The supreme court, however, never addressed whether the court of appeals was correct in assuming that the policy considerations underlying the narrower rule of negligent misrepresentation are sufficient to justify requiring the plaintiff in these situations to proceed only under that theory.

THE JUSTIFICATION FOR NEGLIGENT MISREPRESENTATION LIABILITY AND THE APPLICABILITY OF THAT JUSTIFICATION TO ARCHITECTS' LIABILITY TO THIRD PARTY CONTRACTORS

This section addresses what the Arizona Supreme Court did not: whether the policy concerns thought to justify the narrow liability of negligent misrepresentation constitute a persuasive justification for affording architect defendants the additional protection of that doctrine. Two social policy concerns underlie the narrower liability rule for negligent misrepresentation. The first is the economic concern of encouraging the flow of commercial information.[84] The second is the concern of limiting the liability of those who prepare and communicate information.[85]

The first policy concern, to encourage the flow of commercial information, does not justify application of the negligent misrepresentation doctrine in the architect context. It is clear that our economy is dependent on the

80. *Id.* at 188, 677 P.2d at 1296.
81. *Id.* at 189, 677 P.2d at 1297.
82. *Id.* at 187, 677 P.2d at 1295.
83. *Id.* at 187-88, 677 P.2d at 1295-96.
84. RESTATEMENT (SECOND) OF TORTS § 552 comment a (1977).
85. *Id.* This concern arises from the perception of "the extent to which misinformation may be, and may be expected to be, circulated and the magnitude of the losses which follow from reliance upon it." *Id.*

free flow of commercial information.[86] Much information, however, is unimportant to most individuals in the system and *mis* information can be harmful to the system. Thus the objection that there is not much to gain by encouraging the flow of negligently prepared information must be addressed. The most obvious rejoinder to this objection is that the negligent misrepresentation doctrine serves to encourage the free flow of *all* commercial information. The expectation, the rejoinder would continue, is that the cost to society of the negligently prepared information is outweighed by the gain to society from the "good" information which might have been lost were the liability rule based on reasonable foreseeability. The reasoning is that those who prepare and communicate information will produce more information if negligent misrepresentation is applied than if reasonable foreseeability negligence is applied and that it makes economic sense to encourage this additional information. More information would be produced because with the narrower misrepresentation standard, liability resulting from faulty information would be less likely.

This argument, however, is not persuasive in the architect context because it rests on an assumption that is false in that context, i.e., the assumption that the benefits resulting from additional good information outweigh the harm resulting from additional bad information. That this utility assumption is not justified in the architect context can be seen through introducing the notion of an information market.[87] There are different types of information which are produced and consumed and, correspondingly, there are different information markets. The market for architectural information is not a market in which the above utility assumption is true. This is illustrated in two ways.

One way contrasts the architectural information market with a market for information having a different content. The science and high technology information market, for example, is a market in which the potential gains from encouraging the production of additional information outweigh the harm caused by the faulty information that would not have reached the market under ordinary negligence liability.[88] In the science/high technology market, the narrower liability of negligent misrepresentation is more appropriate than the broader liability of negligence based on reasonable foreseeability because of the relatively minimal risk of harm to society from faulty information. In contrast, in the market for architectural information society has much to lose—in life, limb, property, and money—from application of the narrower liability of negligent misrepresentation. Moreover, only architects, and not society, stand to gain from applying negligent misrepresentation rather than negligence in the architects' information market. There is the argument that the broader liability of ordinary negligence will result in a

86. *See generally* E. MACKAAY, ECONOMICS OF INFORMATION AND LAW 107-118 (1982).

87. *Id.* at 145 and 113-15.

88. High tech information is likely to be initially employed by high tech industries which will have the resources to confirm the information before putting it to use. Once confirmed and put to use, such high tech information could then manifest itself in gains to society in general. Immediate use of such new high tech information directly by individual members of society less able to evaluate and spread the risk of loss would be unlikely.

shortage of architectural plans and specifications but this is highly unlikely. Architects are far more likely to respond to broader liability rules by buying broader malpractice insurance coverage than by leaving their profession. Moreover, even if there were some shrinking of the profession, surely those remaining would command a higher price for their services; this greater profit would eventually attract new members to the profession.

A key idea in this analysis is that the greater the expected net cost to society of encouraging a free flow of a given type of information, the broader the liability should be for negligently preparing or communicating that information. This idea can not only be applied across different information markets distinguishable by the subject matter (such as high tech versus architectural), but can also be applied to information markets distinguishable in another way, such as markets in which information bears directly on prices of commodities and services. Such information is price information, and it is extremely important to our economy.[89] Since architectural plans and specifications function, in part, to inform bidding contractors how much they would have to spend on labor and materials, those plans and specifications are a type of price information. The flow-of-commercial-information justification for negligent misrepresentation fails to justify its application even when architectural information is viewed as price information.

The market for price information is a market in which the utility assumption is not justified. The liability rule of ordinary negligence plays the important role of deterring inaccurate price information without running any realistic risk of a shortage of accurate price information. The self interest of each individual participant in the system should ensure that he or she acquires the relevant price information from, and passes it on to, those who have an interest in it.[90] Since market forces will ensure that there is enough good information, and since the reasonable foreseeability rule serves the purpose of deterring bad information, there is no reason to encourage additional information which would serve only to increase the amount of bad information. The balance of net social gains over net social costs is not maximized by applying negligent misrepresentation's narrow liability rule to architectural plans and specifications.

The second policy concern which justifies the narrower liability standard of negligent misrepresentation is the concern that without this stan-

89. *See generally* Hayek, *The Use of Knowledge in Society*, 35 AM. ECON. REV. 519 (1945).

90. *Id.* Hayek argues that the price system will serve to disseminate the necessary price information in the necessary way and that a key problem of economic efficiency is how to best utilize information which is spread among the people. *Id.* at 520. Hayek further states that individual participants in our economic system need to know extremely little in order to successfully play their part. *Id.* What little the individual participants do need to know, is conveyed to them via the price system, which is a mechanism for communicating the necessary information in such a way that "only the most essential information is passed on, and passed on only to those concerned." *Id.* at 527. Since the price system is the solution to the important economic problem of how to best utilize relevant information where this information is initially dispersed among many people, it is crucial that inaccurate price information be deterred, provided, of course, that this can be done without diminishing the supply of accurate price information. There does not, however, seem to be any realistic offsetting concern that the reasonable foreseeability negligence rule will, in deterring inaccurate price information, result in a shortage of accurate price information. Market forces should ensure that those who need the relevant information have it. *See id.* at 525-27 for a hypothetical illustration.

dard, those who prepare and communicate information are potentially subject to unlimited liability. Justice Cardozo voiced this concern in *Ultramares v. Touche*.[91] *Ultramares* involved an investor's economic loss from relying on a negligently certified balance sheet prepared by the defendant accountants. Justice Cardozo expressed the need to avoid imposing "liability in an indeterminate amount for an indeterminate time to an indeterminate class."[92] This fear of unlimited liability, however, is not always realistic. Where it is not, there may be no justification for the limited liability of negligent misrepresentation. The Illinois Supreme Court recognized this in *Rozny v. Marnul*,[93]

In *Rozny*,[94] a surveyor inaccurately surveyed a vacant lot and was held liable to a third party who detrimentally relied on the survey in financing and purchasing the property. The court declined to strictly apply *Ultramares*, reasoning that the potential liability was not that extreme given that the class of persons who might foreseeably be injured was narrowly limited and that injury would ordinarily occur only once.[95]

Although the *Rozny* court emphasized the fact that the surveyor had voluntarily placed an "absolute guarantee" on the plat, other considerations contributing to the court's holding were the promotion of precautionary techniques among surveyors and the "undesirability" of forcing an innocent party to bear the burden of a professional's mistakes.[96] These same considerations, as well as the professional's better position to more fairly and easily spread the risk of loss, led the United States District Court of Rhode Island to conclude in *Rusch Factors, Inc. v. Levin*[97] that "the decision in *Ultramares* constitutes an unwarranted inroad upon the principle that '[t]he risk reasonably to be perceived defines the duty to be obeyed.' "[98]

Taken together, *Rusch* and *Rozny* suggest that where the potential liability is not great, the fear of unlimited liability should give way to concerns of deterrence, risk spreading, and the injustice of having an innocent party bear the burden of a professional's mistakes. In third party contractors' suits against architects for economic loss caused by negligently prepared plans, the class of persons who might foreseeably be injured by the information is narrowly limited. Moreover, injury would ordinarily occur only once because the victim would likely inform the architect of the defects upon discovery. In such a situation, tort law's broad concerns with compensating

91. 255 N.Y. 170, 174 N.E. 441 (1931).
92. *Id.* at 173, 174 N.E. at 444.
93. 43 Ill. 2d 54, 250 N.E.2d 656 (1969).
94. The facts in *Rozny* are set out in 43 Ill. 2d at 56-59, 250 N.E.2d at 657-59.
95. The court stated:

> The situation is not one fraught with such an overwhelming potential liability as to dictate a contrary result, for the class of persons who might foreseeably use this plat is rather narrowly limited, if not exclusively so, to those who deal with the surveyed property as purchasers or lenders. Injury will ordinarily occur only once and to the person then owning the lot.

Id. at 66, 250 N.E.2d at 662.
96. *Id.* at 67-68, 250 N.E.2d at 663.
97. 284 F. Supp. 85, 91 (D.R.I. 1968).
98. *Id.* at 91, *quoting Palsgraf*, 248 N.Y. at 344, 162 N.E. at 100.

innocent parties for another's fault, as well as considerations of deterrence, risk spreading, and justice, require liability.

It is proposed that where a third party suffers economic loss in reliance on an architect's faulty plans and specifications, concern over compensating the innocent contractor for the architect's negligence and considerations of deterrence, risk spreading, and justice should override fear of unlimited liability and the concern with the free flow of commercial information. The burden should be placed on the architect to plead and prove that in his or her case there is a reasonable fear of unlimited liability.[99] If the architect defendant meets this burden, negligent misrepresentation should be applied. If the architect cannot meet this burden, larger policy concerns require the architect to face the reasonable foreseeability rule.

CONCLUSION

Architects' liability to third party contractors for economic loss resulting from negligently prepared plans and specifications has expanded over the years. Recovery in this context, however, is generally unavailable under theories of implied warranty and strict liability and is severely limited under third party beneficiary theory. Contractors, however, can now recover under some version of negligence. This recovery is unhampered by the broad form of the English immunity rule and by the privity defense.

Negligence, rather than negligent misrepresentation, will generally be the more appropriate theory of recovery. The two policy concerns underlying the narrower liability rule for negligent misrepresentation fail to justify a general rule requiring contractors to proceed under that theory. It is proposed that if an architect can plead and prove a reasonable fear of unlimited liability, then negligent misrepresentation is an appropriate theory. If this burden is not met, then tort law's broad concerns with compensation, deterrence, risk spreading, and justice require that the architect be subject to reasonable foreseeability negligence.

99. Such a burden might be met by an architect, who, for example, has been paid to supply plans to a national chain of hardware stores for the construction of a vacation cabin where such plans are to be sold to "do-it-yourselfers."