Recovery in Tort for Purely Economic Loss: Contract Law on the Retreat

NICHOLAS RAFFERTY*

This paper focuses upon the influence traditionally exercised by contract law in precluding recovery in tort for purely economic loss and shows how this influence is now declining. It examines tortious liability for purely economic loss in two principle areas, liability for the negligent performance of a service voluntarily undertaken and liability for the negligent production of a defective chattel or building. In both areas there are increasing signs that tortious liability is being used both as an alternative to contractual liability in certain situations and as a means of expanding the recognized scope of contractual liability.

L'article qui suit examine l'influence que le droit des contrats a traditionnellement exercée en empêchant l'indemnisation du préjudice purement économique sur le fondement de la responsabilité délictuelle et démontre que cette influence est en train de disparaître. L'auteur étudie la responsabilité délictuelle en cas de préjudice purement économique dans deux domaines principaux, à savoir en cas d'exécution négligente d'un service librement fourni et en cas de production négligente d'un objet ou immeuble défectueux. Dans ces deux secteurs, on constate que l'on invoque de plus en plus la responsabilité délictuelle tant en remplacement de la responsabilité contractuelle dans certains cas que comme moyen d'élargir le champ reconnu de la responsabilité contractuelle.

This paper does not attempt to deal comprehensively with the problem of recovering purely economic loss in the tort of negligence.[1] It focuses instead upon the influence exercised by contract law in precluding recovery in tort for purely economic loss and shows how this influence is on the wane.

Contract law's sway affected two related situations. First, it was recognized until recently that, where two parties were in a contractual relationship,

*Professor, Faculty of Law, University of Calgary.

[1]There have been a number of recent excellent treatments of the subject: J.A. Smillie, "Negligence and Economic Loss" (1982), 32 *U.T.L.J.* 231; J.A. Feldthusen, *Economic Negligence: The Recovery of Pure Economic Loss* (Toronto: Carswell, 1984); J.C. Smith, "Economic Loss and the Common Law Marriage of Contracts and Torts" (1984), 18 *U.B.C.L. Rev.* 95; J.C. Smith, *Liability in Negligence* (Toronto: Carswell, 1984), esp. chs. 4-6; and J. Blom, "The Evolving Relationship between Contract and Tort" (1985), 10 *C.B.L.J.* 257.

no action in tort would lie for one party's negligent performance of that contract in so far as any damage caused was purely economic. Where the plaintiff's complaint was that the defendant had failed to do properly the very matters he had contracted to do, any action had to be founded in contract alone. If for any reason, such as the expiry of a limitation period, an action in contract was unavailable, tort law could not come to the plaintiff's assistance. Lord Diplock made this point very clearly in 1964 in *Bagot* v. *Stevens Scanlan & Co.*[2] when dealing with the liability of an architect to his contractual client:

> It seems to me that, in this case, the relationship which created the duty on the part of the architects towards their clients to exercise reasonable skill and care arose out of the contract and not otherwise. The complaint that is made against them is of a failure to do the very thing which they contracted to do. That was the relationship which gave rise to the duty which was broken. It was a contractual relationship, a contractual duty, and any action brought for failure to comply with that duty is, in my view, an action founded on contract. It is also, in my view, an action founded on contract alone.[3]

As will be seen in the following pages, this narrow approach has now been discarded in favour of a general recognition of tortious liability between contracting parties. The existence of a contract, therefore, no longer automatically excludes a potential claim in tort. It will also be seen that the availability of tortious liability between contracting parties is just part of a wider principle to the effect that a party who undertakes to perform a service for another in a business or professional context, upon which undertaking that other party relies, will be liable in tort to that other party for any economic loss caused by his negligent performance of, or failure to perform, the service undertaken.[4] This principle applies whether or not there is a contract between the parties and, it is submitted, whether or not the defendant's negligence takes the form of misfeasance or nonfeasance. The imposition of tortious liability in such circumstances, therefore, diminishes the importance of consideration.

The principle has been carried further so as to strike at the doctrine of privity of contract. Thus, a defendant who is under contract to and working for one party to a transaction may at the same time be held to have undertaken to perform a service for the plaintiff, another party to the same transaction. If the plaintiff relies upon such an undertaking and suffers loss because of the defendant's negligent failure to honour his undertaking, then liability will flow. The furthest application of the principle has been in circumstances where it cannot be said that the defendant has given any undertaking to the plaintiff at all, but where the defendant has given an undertaking (normally by contract) to some third party to perform a service of which the plaintiff is a

[2][1966] 1 Q.B. 197.

[3]*Ibid.*, at 204.

[4]Smillie, *supra*, footnote 1 at 233, expresses the principle in the following terms: "[A] defendant who undertakes to perform a business or professional service a principal object of which is to protect or advance the plaintiff's economic interests will be liable to the plaintiff for purely economic loss caused by negligent performance of or failure to perform that service." Feldthusen, *supra*, footnote 1 at 138, uses similar language to define the principle: "[T]he defendant will be held liable for the plaintiff's economic loss if: (1) the defendant voluntarily undertakes to perform a specific service for the plaintiff's benefit, (2) the plaintiff relies on the defendant to perform the undertaking, and (3) the negligent performance of the service injures the plaintiff."

beneficiary. In these circumstances, too, the courts have been prepared to recognize a duty of care despite the fact that, by so doing, they are arguably subverting the doctrine of privity. The first part of this paper analyzes this principle of liability in order to consider the extent to which it has been accepted by the courts, the effect it has had upon contractual theory and its future development.

The second area in which contract law has played a significant role in denying recovery in tort for purely economic loss is that of products liability. The situation to be considered is as follows: the parties are not in a contractual relationship but the plaintiff has acquired, through a contract with a third person, a defective chattel or building which has been negligently produced by the defendant. Developments have not been so extensive in this context. Until *Donoghue* v. *Stevenson*[5] contractual theory prevented a claim in tort against a manufacturer even for personal injuries and this decision was not fully extended to realty until much more recently.[6] It is, therefore, not surprising that it is still very much the position that any claims for defects in the product itself or for consequential economic losses, such as losses of profits suffered while the product is being repaired, sound only in contract against the supplier and not in tort against the producer. The basis of a plaintiff's claim in such a case is said to be that the product is not of the quality which the plaintiff expected. A claim for such lost expectations is said to be a claim in contract and can be brought only against the party who created those expectations, namely the contractual supplier, and not against the remote producer. Tortious liability can be imposed only where a product is not only defective but also dangerous and, even then, only where the product has caused personal injuries to, or damage to some other property of, the plaintiff.

Despite this traditional view of the relationship of contract and tort, the law in this area is in a state of flux and the inroads which have been made into the traditional position form the basis of the second part of this paper. There is now a group of cases to the effect that a producer can be liable to a consumer for the cost of repairing dangerous defects in chattels or buildings and for economic losses consequential upon such repairs. There is no requirement in these cases for the product to have caused personal injuries or damage to other property before liability can be imposed. There are even some decisions which suggest that a manufacturer or builder can be tortiously liable for the cost of repairing, and for consequential economic losses in respect of, a product which is unmerchantable but not dangerous in any way. In this context, the most important decision is the recent one of the House of Lords in *Junior Books Ltd.* v. *Veitchi Co. Ltd.*,[7] which will be considered in full below.

It will be argued that, while tort law has a part to play with respect to dangerous products, there are problems with extending tortious liability to products which are defective but safe. Such reforms as are desirable are best

[5][1932] A.C. 562 (H.L.).

[6]See *e.g.*, *Lock and Lock* v. *Stibor* (1962), 34 D.L.R. (2d) 704 (Ont. H.C.); *Dutton* v. *Bognor Regis U.D.C.*, [1972] 1 Q.B. 373 (C.A.); *Anns* v. *London Borough of Merton*, [1977] 2 All E.R. 492 (H.L.).

[7][1982] 3 W.L.R. 477 (H.L.).

achieved through legislation; as will be seen, the process of legislative change has already begun.

NEGLIGENT PERFORMANCE OF, OR FAILURE TO PERFORM, A SERVICE VOLUNTARILY UNDERTAKEN[8]

Parties Are in a Contractual Relationship

Where one contracting party wishes to sue the other in tort for that other's negligent performance of the contract, little difficulty has been encountered where physical damage has been caused. Doctors, dentists and cleaners of chandeliers have all been held liable in tort in such circumstances.[9] In so far as any loss caused was purely economic, however, the plaintiff, until recently, would have been met with the proposition that any liability had to sound in contract alone. Solicitors in particular were singled out as being liable to their clients in contract only.[10] The exclusivity of contract rested on no secure historical foundations. Thus in the middle of the last century, in *Boorman* v. *Brown*,[11] Tindal C.J. said:

> That there is a large class of cases in which the foundation of the action springs out of privity of contract between the parties, but in which, nevertheless, the remedy for the breach, or non-performance, is indifferently either assumpsit or case upon tort, is not disputed. Such are actions against attorneys, surgeons, and other professional men, for want of competent skill or proper care in the service they undertake to render: actions against common carriers, against ship owners on bills of lading, against bailees of different descriptions: and numerous other instances occur in which the action is brought in tort or contract at the election of the plaintiff.... The principle in all these cases would seem to be that the contract creates a duty, and the neglect to perform that duty, or the nonfeasance, is a ground of action upon a tort.[12]

Unfortunately the *Boorman* principle had a short reign and it soon became accepted that no tortious liability would be available in these circumstances.

The catalyst for change proved to be the influential decision of the House of Lords in 1963 in *Hedley Byrne & Co. Ltd.* v. *Heller & Partners Ltd.*[13] That case recognized tortious liability, in limited situations, for negligent misstatements or advice causing purely financial loss. The major difficulty facing the court was the isolation of the circumstances in which a duty of care

[8]See generally Smillie, *supra*, footnote 1 at 254-80 and Feldthusen, *supra*, footnote 1 at 137-75.

[9]*E.g.*, *Edwards* v. *Mallan*, [1908] 1 K.B. 1002 (C.A.); *Parmley* v. *Parmley*, [1945] S.C.R. 635; *Fish* v. *Kapur*, [1948] 2 All E.R. 176 (K.B.D.); *Dominion Chain Co. Ltd.* v. *Eastern Construction Co. Ltd.* (1976), 68 D.L.R. (3d) 385 at 409-410 (C.A.) *per* Wilson J.A.; *Jackson* v. *Mayfair Window Cleaning Co. Ltd.*, [1952] 1 All E.R. 215 (C.A.).

[10]*E.g.*, *Groom* v. *Crocker*, [1939] 1 K.B. 194 (C.A.); *Clark* v. *Kirby-Smith*, [1964] 1 Ch. 506; and *Messineo* v. *Beale* (1978), 20 O.R. (2d) 49 (C.A.). See also the influential decision of Laskin J.A. in *Schwebel* v. *Telekes*, [1967] 1 O.R. 541 (C.A.), which dealt with the liability of a notary public. See generally, N. Rafferty, "The Tortious Liability of Professionals to their Contractual Clients" in Steel and Rodgers-Magnet (ed.), *Issues in Tort Law* (Toronto: Carswell, 1983) 243-63.

[11](1842), 3 Q.B. 511, 114 E.R. 603 (Ex. Ch.).

[12]*Ibid.*, at 525-26 (Q.B.), 608-609 (E.R.). *Boorman* v. *Brown* was affirmed in the House of Lords (1844), 11 Cl. & F. 1, 8 E.R. 1003, where Lord Campbell said at 44 (Cl. & F.), 1018-19 (E.R.): "[W]herever there is a contract and something to be done in the course of the employment which is the subject of that contract, if there is a breach of duty in the course of that employment, the plaintiff may recover either in tort or in contract."

[13][1964] A.C. 465 (H.L.).

should arise in respect of negligent words. It was unwilling to apply the "neighbour principle" of *Donoghue* [illegible][14] because of fears of indeterminate liability. Before liability could issue, there had to be an indication that the speaker had assumed some responsibility for the accuracy of what he said.[15] It was clear, however, that the professional advisor would be the typical person to attract a duty of care under the new *Hedley Byrne* doctrine.[16]

At first glance, *Hedley Byrne* offered little indication of the substantial changes in the law that it would achieve over time. First, there was no contractual relationship between the parties in *Hedley Byrne*. Indeed the major importance of the case lay in opening up avenues of relief where none existed previously precisely because there was no contract. To restrict *Hedley Byrne* to non-contractual relationships, however, would lead to the anomalous result that a third party could sue in tort and obtain the advantage of, for example, the later commencement of a limitation period, whereas the defendant's contractual client would be limited to his contractual remedies. There were, however, indications in *Hedley Byrne* that this form of tortious liability should equally be applicable to contracting parties.[17] Lord Devlin, for example, spoke of the need to find a relationship " 'equivalent to contract',[18] that is, where there is an assumption of responsibility in circumstances in which, but for the absence of consideration, there would be a contract".[19] Indeed, he regarded the presence of consideration as an important factor in the imposition of a duty of care.[20] Above all, the examples he gave of general relationships which would attract a *Hedley Byrne* duty of care were the contractual relationships of solicitor and client and banker and customer:

> I shall therefore content myself with the proposition that wherever there is a relationship equivalent to contract, there is a duty of care. Such a relationship may be either general or particular. Examples of a general relationship are those of solicitor and client and of banker and customer.... Where there is a general relationship of this sort, it is unnecessary to do more than prove its existence and the duty follows.[21]

Secondly, *Hedley Byrne* concerned tortious liability for negligent misstatements made by professionals. A broad view can, however, be taken that *Hedley Byrne* covers all forms of negligent provision of professional and other services. There is no logical reason why it should not extent to negligent acts or even omissions occasioning purely economic loss in a professional or even a straight business context. The judgment of Lord Morris certainly supported the application of *Hedley Byrne* beyond the area of negligent misstatments. He said:

[14] *Supra*, footnote 5.

[15] *Supra*, footnote 13 at 483 *per* Lord Reid and at 529-30 *per* Lord Devlin.

[16] This was true even of the later restriction of *Hedley Byrne* by the Privy Council in *Mutual Life Assurance Co. v. Evatt*, [1971] A.C. 793 (P.C.) (N.S.W.).

[17] See, C.R. Symmons, "The Problem of the Applicability of Tort Liability to Negligent Misstatements in Contractual Situations: A Critique on the Nunes Diamonds and Sealand Cases" (1975), 21 *McGill L.J.* 79, at 90-97.

[18] *Nocton v. Lord Ashburton*, [1914] A.C. 932 at 972 (H.L.) *per* Lord Shaw.

[19] *Supra*, footnote 13 at 529.

[20] *Id.*

[21] *Ibid.*, at 530.

> My Lords, I consider that it follows and that it should now be regarded as settled that if someone possessed of a special skill undertakes, quite irrespective of contract, to apply that skill for the assistance of another person who relies upon such skill, a duty of care will arise.[22]

For a long time, however, the courts acted as if *Hedley Byrne* was of limited application. Even in the area of professional liability, it was felt that *Hedley Byrne* could have no application to contracting parties and that its scope could not extend beyond negligent misstatements in the strict sense.[23] These cases culminated in Canada with the infamous *dicta* of Pigeon J. in *J. Nunes Diamonds Ltd.* v. *Dominion Electric Protection Co.*[24]:

> [T]he basis of tort libability considered in *Hedley Byrne* is inapplicable to any case where the relationship between the parties is governed by a contract, unless the negligence relied on can properly be considered as "an independent tort" unconnected with the performance of that contract....[25]

The first major loosening of contract's stranglehold came with the English Court of Appeal decision in *Esso Petroleum Co. Ltd.* v. *Mardon.*[26] One of the issues in that case was whether Esso could be liable under *Hedley Byrne* for the negligent misstatements of its representatives which had induced Mardon to enter into a lease of a service station with Esso. The case, therefore, did not concern the provision of services generally nor the negligent performance of a contract; rather, it dealt with liability for pre-contractual misstatements. However, Esso, relying on *Clark* v. *Kirby-Smith*,[27] argued that the rights and duties of the parties were governed by the ensuing contract and that there was no place for the law of tort in that contractual relationship. Lord Denning M.R. rejected the *Clark* case and, for good measure, also rejected *Bagot* v. *Stevens Scanlan & Co.*[28] and *Groom* v. *Crocker*[29]. Going back to *Boorman* v. *Brown*,[30] he concluded that "in the case of a professional man, the duty to use reasonable care arises not only in contract, but is also imposed by the law apart from contract, and is therefore actionable in tort".[31]

Esso was followed by the majority of the Ontario Court of Appeal in *Dominion Chain Co. Ltd.* v. *Eastern Construction Co. Ltd.*,[32] who held that an engineering firm was liable to its client in tort for the negligent fulfilment of its contract. To reach that conclusion, however, the Court did not rely on

---

[22] *Ibid.*, at 502-503.

[23] See *e.g.*, *Clark* v. *Kirby-Smith*, *supra*, footnote 10.

[24] [1972] S.C.R. 769.

[25] *Ibid.*, at 777-78.

[26] [1976] Q.B. 801 (C.A.).

[27] *Supra*, footnote 10.

[28] *Supra*, footnote 2.

[29] *Supra*, footnote 10.

[30] *Supra*, footnotes 11 and 12.

[31] *Supra*, footnote 26 at 819.

[32] *Supra*, footnote 9, aff'd, without considering this point *sub nom. Giffels Associations Ltd.* v. *Eastern Construction Co. Ltd.*, [1978] 2 S.C.R. 1346.

Hedley Byrne directly but preferred to base its decision upon an expansion of the class of the old common callings to include all those who "profess skills in a calling which a reasonable man would rely on".[33]

The major breakthrough was achieved by Oliver J. in *Midland Bank Trust Co. Ltd.* v. *Hett, Stubbs & Kemp*[34] where the importance of *Hedley Byrne* was fully appreciated. One issue there was whether a solicitor could be liable in tort to his client for negligently failing to register an option so as to protect his client's interest. The judge was in no doubt that *Hedley Byrne* could not logically be confined to non-contractual relationships. He was also quite clear in his own mind that the principle underlying *Hedley Byrne* could easily be extended to a situation, such as the one before him, involving the negligent provision of professional services.[35] He said:

> Nor, as I read the decision [*Hedley Byrne*], can its operation be confined to cases where the service undertaken takes the form of a representation or of a statement of fact or opinion, or advice. It must logically, I think, apply where the service involves some other positive action such as the giving of a notice .... Once the duty is established it cannot, in my judgment, matter whether the breach takes the form of malfeasance or nonfeasance....[36]

To like effect is the opinion of Nemetz C.J. in *Tracy* v. *Atkins*,[37] where he said:

> It is true that *Hedley Byrne* dealth with negligence arising from the giving of advice. *A fortiori* it is my opinion that in cases of negligence arising from the giving of legal services the same rationale should apply. I should add that in my view the special relationship said to arise when one party relies on the skill of another who undertakes to apply that skill for his assistance is no more than a particular way of establishing a degree of proximity on which a duty of care may be founded.[38]

The importance of decisions like *Midland Bank* lies not just in the fact that tortious remedies are now available between contracting parties but also in the fact that negligent acts — and, it seems, omissions — as opposed to statements, causing purely economic loss can give rise to a liability in tort. These cases thus create a large hole in the supposed exclusionary rule which denies recovery in tort for purely economic loss, while signifying the declining influence of contract law.

The full significance of cases like *Midland Bank* has not always been appreciated by later courts, with the result that they have sometimes made matters more difficult for themselves than they need be. A good example of this tendency is the decision of the Alberta Court of Appeal in *Canadian Western Natural Gas Co. Ltd.* v. *Pathfinder Surveys Ltd.*[39] That case concerned the

[33] *Ibid.*, at 392 *per* Jessup J.A.

[34] [1979] 1 Ch. 384.

[35] See K.M. Stanton, "Solicitors and Professional Liabilities: A Step Forwards" (1979), 42 *Mod. L. Rev.* 207.

[36] *Supra*, footnote 34 at 416.

[37] (1979), 105 D.L.R. (3d) 632 (B.C.C.A.).

[38] *Ibid.*, at 638.

[39] (1980), 12 Alta. L.R. (2d) 135 (C.A.) See also *Vardog Construction Ltd.* v. *Coulthard & Associates Engineering Ltd.* (1980), 36 A.R. 187 (Q.B.).

liability of the defendant survey company to the plaintiff gas company to whom the defendant was under contract, for negligently surveying and staking the route for a proposed natural gas pipeline. The plaintiff was forced to relocate a section of the line because it fell outside the plaintiff's right of way and conflicted with plans for a future City of Calgary water line. The plaintiff sued the defendant for the cost of relocation; the question arose as to whether the defendant could be liable in tort as well as in contract. If the Court had adopted a broad view of *Hedley Byrne*, the issue should have been resolved easily. The defendant had undertaken to perform a service for the plaintiff in a professional context. The plaintiff had relied on the defendant to fulfill its undertaking. The defendant had carried out the service negligently and damage had been caused to the plaintiff. Liability should, therefore, have flowed in tort despite the economic nature of the plaintiff's loss.

Unfortunately, the Court followed a much more complicated path to reach the conclusion that the defendant was liable to the plaintiff in tort. First, it felt constrained to apply the "independent tort" test of Pigeon J. in *Nunes Diamonds*.[40] However, the Court was able to find that the defendant owed a duty of care to the plaintiff, independent of any contractual duty, on the basis of the "neighbour principle" of *Donoghue* v. *Stevenson*.[41] Prowse J.A. said:

> [T]he duty of care set out in *Donoghue* v. *Stevenson* ... is not a contractual duty nor does it arise by virtue of there having been a contract between the parties or between one of the parties and another. The duty arises from proximity and neighbourhood.... This is a duty independent of contract....[42]

This reasoning, however, is difficult to swallow because the basis of the plaintiff's claim was that the defendant had performed its contractual obligation negligently. It is hard to view such negligence as being independent from the contract when it was committed in the very performance of the contract.[43] Furthermore, by treating the case as one of products liability rather than one of professional negligence, the Court was faced with the problem discussed in the second part of this paper, namely that purely economic loss is not generally recoverable in tort from a manufacturer. In particular, the Court had to find some way of distinguishing the Supreme Court of Canada decision in *Rivtow Marine Ltd.* v. *Washington Iron Works*[44].

In *Rivtow Marine*, as will be seen, the majority of the Supreme Court held that a manufacturer of defective goods could not be liable under *Donoghue* v. *Stevenson* for the cost of repairing those goods or for loss of profits incurred while repairs were taking place. Such liability was contractual in origin and therefore could not be enforced against the manufacturer by a non-contracting party. It was recognized in *Rivtow Marine* that there could be recovery against a manufacturer where a defective product had caused personal injuries or damage to property other than the product in question. Prowse J.A. in

[40] *Supra*, footnote 24.

[41] *Supra*, footnote 5.

[42] *Supra*, footnote 39 at 151.

[43] See generally J. Irvine, "Comment" (1980), 12 C.C.L.T. 256.

[44] (1974), 40 D.L.R. (3d) 530 (S.C.C.).

Pathfinder Surveys fastened upon this point to find the defendant liable in tort. He determined that the claim was not in respect of a defect in the product of the contract (the survey) but for the consequential loss of other property which the plaintiff suffered as a result of the defendant's negligence. The other property damaged was the rest of the pipeline which the plaintiff could not use unless the portion in question was moved back to its original alignment. He concluded that *Rivtow Marine* would have allowed recovery for such consequential losses.[45] It is submitted that the *Pathfinder Surveys* decision is not consistent with *Rivtow Marine* because the damage to other property contemplated in *Rivtow Marine* was some physical property damage; yet there was no physical damage to the pipeline. The important point, however, is that the Alberta Court of Appeal would never have been confronted with *Rivtow Marine* if it had been prepared to apply the broad principle underlying *Hedley Byrne*.

All the cases considered to this point have concerned the liability of professionals in the strict sense. There is no reason, however, for liability to be so limited. The tort of negligent misstatement is not restricted to professionals;[46] equally, the broader principle to be extracted from *Hedley Byrne* need not be so confined. While liability should not be limited to professionals, it would not normally be appropriate to impose liability, outside of at least the business context, because of the difficulty of establishing that the defendant was undertaking to use due care in the provision of a service for the plaintiff's benefit and that the plaintiff was reasonably relying upon the defendant's undertaking. No such problem is presented by the cases discussed in this section because, in all of them, the parties are in a contractual relationship and hence automatically in some kind of business relationship.

The recent case of *John Maryon International Ltd.* v. *New Brunswick Telephone Co. Ltd.*[47] concerned the liability of engineers for professional negligence. The question arose as to whether the engineers could be liable in tort as well as in contract for what was arguably purely economic loss. The defendants had been engaged by the plaintiff as consulting and design engineers on the construction of a tower for the transmission of microwaves. Through their combined negligence, a tower was built which later required substantial repairs. After a thorough review of the case law, both Canadian and English, the Court held that the defendants could be liable in tort. In coming to this conclusion, the Court could have relied simply on cases like *Dominion Chain*[48] and confined such tortious liability to professionals. The Court, however, expressly rejected any such limitation and said that the principle it

[45] *Supra*, footnote 39 at 152.

[46] *E.g.*, *Nelson Lumber Co. Ltd.* v. *Koch*, [1980] 4 W.W.R. 715 (Sask. C.A.).

[47] (1982), 141 D.L.R. (3d) 193 (N.B.C.A.). See D.K. Allen, "Concurrent Liability With Interest" (1984), 10 *Queen's L.J.* 183; and M.H. Ogilvie, "*John Maryon International Ltd.* v. *New Brunswick Telephone Co. Ltd.*: Some Notes Toward an Obligations Theory of Concurrent Liability in Contract and Tort" (1984), 10 *Queen's L.J.* 193. See also *Doiron* v. *La Caisse Populaire D'Inkerman Ltee.* (1985), 32 C.C.L.T. 73 (N.B.C.A.), where La Forest J.A., following *John Maryon*, had no doubt that the liability of a solicitor to his client could sound concurrently in contract and tort. He said at 87 that "where a breach of contract arises out of negligence, action may be brought concurrently in tort and in contract".

[48] *Supra*, footnote 9.

was advocating extended to professionals and non-professionals alike. It laid down a general rule that a party to a contract who suffers damage from the other's negligent performance of that contract can sue in tort as well as for breach of contract, provided, of course, that the terms of the contract do not purport to exclude either or both forms of liability. La Forest J.A., delivering judgment for the Court, said:

> [I]f a person fails to perform a duty of care he owes to another person, he should not be absolved from the performance of that duty simply because the failure to perform that duty will also result in his failure to perform a contract, unless, of course, he absolves himself by his contract against liability flowing from his failure to perform that duty.[49]

At another point in his judgment La Forest J.A. said:

> [T]he views adopted here would not displace the rights of the parties to a contract to apportion liability as they see fit. All that is done is to give effect to a duty imposed by law on a person who undertakes certain activities. Whether he has undertaken them by virtue of contract is immaterial, except that this may also result in his being liable for breach of his contract as well as in tort, and that he may by virtue of a term in the contract be absolved from both contractual and tortious liability.[50]

John Maryon, therefore, offers some support for the view that professionals do not constitute the only class of persons who can be liable in tort for purely economic loss when in a contractual relationship with the plaintiff. For its conclusion, however, the Court did not rely on a broad view of *Hedley Byrne*; it preferred to rely on an application of *Donoghue* v. *Stevenson*[51]. As with the *Pathfinder Surveys*[52] case, such a reliance on *Donoghue* immediately raises the problem of the purely economic nature of the loss. The Court, however, never addressed that problem directly. Without adopting *Hedley Byrne*, it is difficult to see why the defendants should have owed the plaintiff any duty of care in tort.[53] In *Rempel* v. *Parks*,[54] Lambert J.A., in a dissenting judgment, agreed with La Forest J.A. that concurrent liability in contract and tort for purely economic loss was not restricted to particular callings or professions. He held that a sheriff was liable to a solicitor for failing to exercise reasonable care in serving a writ on behalf of the solicitor. He should have warned the solicitor of the difficulty he was having in serving the writ to permit the solicitor to take other steps to serve the writ, or to have it renewed, before it expired. The sheriff's liability could be enforced in contract or in tort. Unlike La Forest J.A., however, Lambert J.A. saw the sheriff's liability in tort as flowing ultimately from *Hedley Byrne*.

It is interesting to speculate upon the classes of persons who might attract tortious liability under the principle being discussed. In particular, where the service takes the form of the erection of a building for the plaintiff or of some

[49] *Supra,* footnote 47 at 221.

[50] *Ibid.*, at 225.

[51] *Supra,* footnote 5.

[52] *Supra,* footnote 39.

[53] Similar problems are raised by *Batty* v. *Metropolitan Property Realizations Ltd.*, [1978] 1 Q.B. 554 (C.A.) as regards the plaintiff's action in tort against the first defendant, a development company.

[54] [1984] 4 W.W.R. 689 (B.C.C.A.).

improvement to an existing building owned by the plaintiff, and the building or improvement is shoddily constructed, can the plaintiff recover from the contractor in tort for the cost of repairs and for any consequential economic losses? This question has not arisen often because normally the plaintiff's contractual remedies will be adequate. Where it has arisen, the situation has traditionally been treated in the same way as products liability cases and the courts have had to face the difficulties posed by *Rivtow Marine*.[55] This was the approach taken, for example, by the Ontario Court of Appeal in the *Dominion Chain*[56] case. One of the issues raised there was whether a builder was liable in tort to the owner for the cost of repairing the roof of a factory which the builder had negligently constructed. The roof had leaked, thereby damaging some of the equipment in the factory. The Court applied *Donoghue* v. *Stevenson* and was then forced to distinguish *Rivtow Marine*. It did so on a number of spurious grounds. It said, for example, that in *Dominion Chain,* unlike *Rivtow Marine*, "there was property damage, other than to the 'article' itself".[57] It is true that the defective roof had led to some damage to the factory equipment. It does not, however, follow from *Rivtow Marine* that the cost of repairs to the manufactured article can be recovered just because property damage caused by the manufacted article can be recovered.[58] In *Dominion Chain* the cost of the repairs to the roof was some 30 times greater than the damage caused to the factory equipment. As one commentator has pointed out, "the figures themselves suggest that the consequential loss claim as a basis to support recovery for the cost of repairs might be seen as a case where the tail is wagging the dog".[59]

It is submitted that cases like *Dominion Chain* could more readily be decided on the same basis as that underlying cases like *Midland Bank*[60]. The defendant has undertaken, by contract, to perform a service for the plaintiff, the plaintiff has relied on the defendant's undertaking and has suffered loss as a result of the defendant's negligent performance of the service. There is no need to treat the case as if it were one of products liability.[61] Perhaps, different considerations should apply where a plaintiff agrees to purchase from the defendant builder a house in the course of construction and then wishes to sue the defendant for shoddy construction. This situation is more akin to that of products liability. There have, however, been a number of cases where tortious liability has been recognized in such circumstances although in none of them has the court clearly come to grips with the problem of the recovery of purely

[55] *Supra,* footnote 44.

[56] *Supra,* footnote 9.

[57] *Ibid.*, at 398.

[58] See P.B. Annis, "Tort or Contract: The Question of Recovery for Economic Loss" (1981), 13 *Ott. L. Rev.* 469 at 497-98.

[59] *Ibid.*, at 498.

[60] *Supra,* footnote 34.

[61] See *Cynat Products Ltd.* v. *Landbuild (Investment and Property) Ltd.*, [1984] 3 All E.R. 513 (Q.B.D.), where the Court found a builder liable in tort in similar circumstances to *Dominion Claim* and made no reference to the products liability cases.

economic loss.[62] There have even been cases where the purchaser from the builder of a completed house has been able to sue the seller in tort for poor construction.[63]

Given the fact that the parties in the cases discussed in this section are in a contractual relationship, the plaintiff will normally have concurrent causes of action in contract and tort. Often his contractual remedy will be adequate; he will not have to look to the law of tort to come to his aid. Sometimes an exclusion clause in the contract may protect the defendant effectively against both contractual and tortious liability. On other occasions however, the existence of tortious relief may lead to a widely different result from any contractual liability. Often a plaintiff, for example, will seek to establish that a defendant is liable in tort so as to delay the commencement of the relevant limitation period.[64] There are also potential differences in the amounts of damages recoverable by suing in tort rather than contract. It is generally felt, for example, that the test for remoteness is broader in tort than in contract,[65] though the difference may not be as wide as is commonly believed[66]. Sometimes a defendant may favour a finding of tortious liability because it enables him to plead the plaintiff's contributory negligence as a defence[67] or to seek contribution from another defendant liable in respect of the same damage[68]. It makes no sense that such substantial differences should still depend on the nature of the plaintiff's cause of action.[69] It will obviously take the legislatures and the courts a long time to eradicate these differences. For the moment, it is important to observe simply how the barriers to tortious liability, erected by contract law in the nineteenth century, are in the process of being scaled.

Parties Are Not in a Contractual Relationship — Gratuitous Voluntary Undertakings

Clearly, it is not only parties in a contractual relationship who can avail themselves of the principle discussed in the preceding section. Gratuitous undertakings can be the subject of tortious liability, thereby shaking the doctrine of consideration. Good examples of the application of this principle are those cases where the defendant has undertaken to obtain or renew insurance

[62] *E.g., Smith and Smith* v. *Melancon*, [1976] 4 W.W.R. 9 (B.C.S.C.); *Thompson* v. *Plainsman Developments Ltd.* (1981), 19 R.P.R. 226 (B.C. Co. Ct.); and *Ward* v. *Dobson Construction Ltd.* (1983), 24 C.C.L.T. 205 (N.B.Q.B.), aff'd (1983), 50 N.B.R. (2d) 1 (C.A.).

[63] *E.g., Ordog* v. *District of Mission* (1980), 110 D.L.R. (3d) 718 (B.C.S.C.); and *Karod* v. *Lingstrom* (1983), 30 R.P.R. 1 (B.S.C.S.).

[64] See generally N. Rafferty, "The Impact of Concurrent Liability in Contract and Tortious Negligence upon the Running of Limitation Periods" (1983), 32 *UNB LJ* 189.

[65] *The Heron II*, [1969] 1 A.C. 350 (H.L.).

[66] See *H. Parsons (Livestock) Ltd.* v. *Uttley Ingham & Co. Ltd.*, [1978] Q.B. 791 (C.A.); *Asamera Oil Corp. Ltd.* v. *Sea Oil and General Corp.*, [1979] 1 S.C.R. 633; and *Kienzle* v. *Stringer* (1981), 35 O.R. (2d) 85 (C.A.).

[67] *E.g., Canadian Western Natural Gas Co. Ltd.* v. *Pathfinder Surveys Ltd., supra*, footnote 39.

[68] *E.g., Dominion Chain Co. Ltd.* v. *Eastern Construction Co. Ltd., supra*, footnote 9.

[69] Feldthusen, *supra*, footnote 1 at 143, is particularly emphatic on this point: "The current practice, whereby a substantive issue is resolved by pure nominalism is reminiscent of the worst features of the old writ system. Clearly, the facts in cases of this type support a valid cause of action; the point is that they support one cause of action, not two."

coverage for the plaintiff and then carries out his undertaking negligently. One early example of this type of case in Canada was *Baxter* v. *Jones*[70] in 1903. The defendant insurance agent undertook to place additional insurance on the plaintiffs' property and to notify the insurance companies already holding policies of this additional coverage. The defendant failed to send the required notices with the result that the plaintiffs sustained a loss. The defendant was held liable for the negligent performance of his undertaking. Having started upon the performance of his undertaking by obtaining the additional coverage, the defendant could not then fail to send the requisite notices, without at least warning the plaintiffs. Osler J. said:

> To stop when he the defendant had only obtained the insurance was simply to go so far with the business as to cause a direct injury to the plaintiffs if he failed to follow it up by notice to the other insurers and cannot be regarded otherwise than as actionable negligence.[71]

In coming to its conclusion, the Court followed a number of earlier English cases,[72] including the classic case on bailment of *Coggs* v. *Bernard*[73]. It is interesting to note that this line of cases proved influential in *Hedley Byrne*[74] itself.

Baxter has been followed in insurance cases of more recent vintage. In *Myers* v. *Thompson and London Life Insurance Co.*,[75] for example, the defendant life insurance agent undertook gratuitously to effect a conversion of a client's life insurance policy, in accordance with instructions from the client's solicitor, in order to minimize death duties. He failed to act in accordance with the instructions, with the result that extra duties were levied against the estate. The Court held that the defendant was liable to the estate for the extra duties. On the basis of *Baxter*, consideration was not required. The defendant was liable for negligent failure to perform his gratuitous undertaking. To support its conclusion, the Court also relied on *Hedley Byrne*, thus showing the interrelationship of *Hedley Byrne* and the voluntary undertaking cases.

The *Baxter* principle has also been applied in a number of cases where *Baxter* itself was not cited.[76] Its application has not been confined to insurance agents, but its major area of impact has been in the insurance field. In *Reid* v. *Traders General Insurance Co.*,[77] reliance was placed on *Hedley Byrne* to hold a car salesman and his employer liable to the plaintiff purchaser for failing to

---

[70](1903), 6 O.L.R. 360 (C.A.).

[71]*Ibid.*, at 363.

[72]*E.g.*, *Wilkinson* v. *Coverdale* (1793), 1 Esp. 75, 170 E.R. 284 (N.P.); and *Skelton* v. *London & North Western Rlwy. Co.* (1867), L.R. 2 C.P. 631.

[73](1703), 2 Ld. Raym. 909, 92 E.R. 107 (K.B.).

[74]*Supra*, footnote 13 at 526-27 *per* Lord Devlin. This point is made by Smith, "Economic Loss and the Common Law Marriage of Contracts and Torts", *supra*, footnote 1 at 123.

[75](1965), 63 D.L.R. (2d) 476 (Ont. Co. Ct.); aff'd without written reasons on May 2, 1967 by Court of Appeal. See also *Cabot Club Ltd.* v. *Town Council of Clarenville* (1981), 104 A.P.R. 67 (Nfld. S.C.).

[76]*E.g.*, *Fine's Flowers Ltd.* v. *General Accident Assurance Co.* (1977), 81 D.L.R. (3d) 139 (Ont. C.A.); and *Bar-Don Holdings Ltd.* v. *Reed Stenhouse Ltd.* (1983), 24 Alta. L.R. (2d) 248 (Q.B.).

[77](1963), 41 D.L.R. (2d) 148 (N.S.S.C.).

comply with an undertaking to obtain insurance for the vehicle. The salesman, in filling out an insurance application form for the plaintiff, had deliberately misstated a material fact with the result that the insurance was invalidated. In *Kostiuk* v. *Union Acceptance Corp. Ltd.*,[78] the manager of the defendant finance company undertook to obtain complete fire insurance coverage on goods being purchased by the plaintiff pursuant to a conditional sales contract. The manager telephoned an agent of an insurance company giving the required information and told the plaintiff that the insurance had been placed. The finance company was held liable when it later transpired that there was no coverage because the manager had negligently failed to follow up on the telephone call to ensure that coverage had been obtained. The Court, this time relying directly on *Baxter*, said that it was irrelevant whether there was any consideration for the defendant's promise because "there is a duty to perform where the promise is gratuitous and steps have been taken".[79]

Many people would rationalize these decisions by constructing a contract between the parties in order to ground liability. There is no need to invent such a contractual relationship, although clearly the liability being imposed is very close to a contractual liability and often the defendant is liable alternatively for breach of contract.[80] The closeness of contract and tort in this area is well illustrated by *McNeil* v. *Village Locksmith Ltd.*[81] The defendant locksmith was employed by the plaintiff to install a "dead bolt" lock on the front door of the plaintiff's house. The lock, as installed, was useles; the house was burgled. The plaintiff sued for breach of contract and succeeded. Grange J., however, spent his entire judgment showing why tortious liability was appropriate in these circumstances on the basis of a broad interpretation of *Hedley Byrne*. The basis of liability was quite irrelevant to the Court.

There is said to be one remaining distinction between tort and contract in this context. Tortious liability cannot be imposed, it is argued, where a defendant simply does not perform his undertaking at all. To compel a party to comply with his promise, that promise has to be part of a valid contract. In *Skelton* v. *London & North Westn Rlwy. Co.*,[82] Willes J. said: "If a person undertakes to perform a voluntary act, he is liable if he performs it improperly, but not if he neglects to perform it. Such is the decision in *Coggs* v. *Bernard*."[83] The same point was made more recently in the *Kostiuk*[84] case. As a pratical matter, however, it is virtually impossible to draw any meaningful distinction between misfeasance and nonfeasance. Moreover, it is submitted that no attempt should be made to draw any such distinction. The important

[78](1967), 66 D.L.R. (2d) 430 (Sask. Q.B.).

[79]*Ibid.*, at 434.

[80]This seems to have been the case, for example, in *Baxter* v. *Jones*, *supra*, footnote 70; *Fine's Flowers Ltd.* v. *General Accident Assurance Co.*, *supra*, footnote 76, and *Reid* v. *Traders General Insurance Co.*, *supra*, footnote 77. See also, Feldthusen, *supra*, footnote 1 at 140-45.

[81](1981), 35 O.R. (2d) 50 (H.C.).

[82]*Supra*, footnote 72.

[83]*Ibid.*, at 636.

[84]*Supra*, footnote 78 at 434.

aspect to liability is that the plaintiff has relied on the defendant's undertaking; it should not matter whether the defendant negligently performs the service undertaken or negligently fails to perform the service at all. Many of the cases examined to this point show how blurred the distinction is between misfeasance and nonfeasance. *Baxter* itself is very close to the line. The defendant performed part of his undertaking but failed to complete it. The same is true of the *Midland Bank*[85] case discussed earlier. Indeed, in that case, Oliver J. said that it should make no difference whether the defendant's negligence "takes the form of malfeasance or nonfeasance".[86]

The recent decision of the Manitoba Court of Queen's Bench in *Maxey* v. *Canada Permanent Trust*[87] goes some way to imposing tortious liability for nonfeasance. The defendant mortgage company had begun foreclosure proceedings against the plaintiff's property when it noticed the absence in its file of a copy of a fire insurance policy. The defendant wrote to the plaintiff demanding a copy within ten days and made the following ultimatum: "If we have not received same by that time, we will have no alternative but to place insurance and charge the premium to your mortgage."[88] Upon receipt of this letter, the plaintiff paid off the arrears owing under his mortgage and was content for the defendant to insure the property and to charge the premium to the mortgage, as the defendant was entitled to do under the provisions of the mortgage agreement. The plaintiff assumed that the defendant would insure the house in an amount sufficient to cover the mortgage debt for the normal period of one year. In fact, the mortgage company insured its own interest only to the end of the calendar year, with the result that the plaintiff was uninsured when his house burnt down the following year. The plaintiff sued the defendant for the loss he had suffered, saying that he would have insured himself if he had not been misled into believing that the defendant had insured the house for the normal period of one year in an amount sufficient to cover the mortgage debt.

Scollin J. found in the plaintiff's favour. In light of the provisions of the mortgage, the plaintiff was entitled to make the assumption he did make as to what the defendant would do. The judge said that the defendant, by its letter, "induced the plaintiff to rely on it and then failed to carry through and place the insurance apparently promised".[89] He continued:

> [T]he letter means and was reasonably understood by the plaintiff to mean that for the usual period of one year at least, or until further notice to or by him, the company would, at his expense, perform his covenant with the company to the extent of protecting its interest. That being the case, it was negligent of the company to proceed in an entirely different manner without notice to the exposed plaintiff.[90]

---

[85] *Supra*, footnote 34.

[86] *Ibid.*, at 416.

[87] (1983), 26 C.C.L.T. 148 (Man. Q.B.).

[88] *Ibid.*, at 158.

[89] *Ibid.*, at 161.

[90] *Ibid.*, at 162.

The judge was not worred by the fact that, to some extent, this was a case of nonfeasance. Liability was imposed because of the plaintiff's reasonable reliance on the defendant's undertaking. In effect, the Court was awarding damages for the loss suffered by the plaintiff's reasonable reliance on a promise which was not honoured, thus questioning the notion that the doctrine of promissory estoppel cannot be used to create a cause of action.[91]

Scollin J.'s judgment was reversed on appeal.[92] The Appellate Court examined the line of voluntary undertaking cases and concluded in effect that no undertaking had been made by the defendant. The defendant never assumed any duty towards the plaintiff. The relationship between the parties remained that of mortgagor and mortgagee. The defendant was under no obligation, by the mortgage itself, to insure the property in any fashion. It could even decide to place no insurance on the property at all. The letter sent to the plaintiff did not alter that existing position. Philp J.A. said:

> It was a letter to its mortgager in default. The Permanent did not indicate to Maxey the type of insurance coverage it would place, or the amount or the term of the coverage. And for his part, Maxey did not make inquiries as to the particulars of the insurance. Nor did he communicate to the Permanent his decision to have the Permanent place insurance coverage on the property.[93]

In light of the plaintiff's failure to communicate with the defendant, there was no reason for the defendant to know that the plaintiff was relying on the defendant to perform the plaintiff's obligation to insure the property.[94] The plaintiff was the author of his own misfortune.

While this aspect of the decision can be accepted, it is unfortunate that the Court of Appeal also intimated that a simple failure to perform an undertaking would never be sufficient to give rise to liability in the absence of consideration. Philp J.A. said:

> The principle applies where a person undertakes to perform a voluntary act and takes steps to perform his undertaking.... The relationship between the parties must be such as to create a trust or other duty which the person has assumed and which he has miscarried.[95]

The decision of the New Zealand Court of Appeal in *Meates* v. *Attorney-General*[96] however, offers encouragement for the view that tortious liability can attach to the negligent failure to perform an undertaking.

Meates was a complicated case arising out of an attempt by the Government of New Zealand to encourage industrial development on the economically depressed West Coast of the South Island. As a result of discussions bet-

[91] See generally J. Irvine, "Annotation" (1983), 26 C.C.L.T. 150.

[92] (1984), 27 C.C.L.T. 238 (Man. C.A.).

[93] *Ibid.*, at 245.

[94] For a similar conclusion, see *Soursos* v. *Canadian Imperial Bank of Commerce*, [1983] 3 W.W.R. 716 (B.C.S.C.).

[95] *Supra*, footnote 92 at 242.

[96] [1983] N.Z.L.R. 308 (C.A.). See E.C.E. Todd, "Negligent Statement, Negligent Conduct and Negligent Promises" (1985), 1 *P.N.* 2.

ween the plaintiffs and the Government, a company called Matai Industries Ltd. was created and several factories were opened. Almost immediately, however, the company encountered financial problems. The Government was adamant that there should be no retrenchment and that the programme of regional development should proceed. A few months later a receiver was appointed. Seven months after that appointment, however, a decision was made to sell the assets of the company. The plaintiffs, who were the shareholders of the company, sued the Government. They claimed that the Government was liable under *Hedley Byrne* for the negligent assurances of its ministers that financial support for the company would be forthcoming and that, if they accepted the appointment of a receiver, their interests would be protected and they would be indemnified against loss. They asserted that they had relied on such assurances by failing to take normal commercial steps to safeguard their position.

One of the main arguments of the defendant was that *Hedley Byrne* could not be applied to undertakings of future action which was not honoured. In the absence of contract, it was submitted that no liability could ensue. The Court, however, summarily rejected that contention. Woodhouse P. and Ongley J. said:

> [A]lthough a promise may fall short of a contractual commitment nonetheless if it is provided by somebody who intends it to be acted upon and who is in an exclusive position to give effect to it, let alone the central Government, then surely it is likely to be received as a far more powerful piece of information than mere opinion whether supplied by a man in a professional capacity or by some other person sufficiently equipped and interested enough in the subject-matter to express a serious view upon it.[97]

Cooke J. also held that mere promises could be the subject of tortious liability. There were occasions when a reasonable person, on receiving such assurances from someone in authority, was entitled to assume that the promisor would take reasonable care to safeguard the interests of those he had sought to influence. In such a case, the promisor would be bound to take all reasonable steps to fulfill his promises.[98] In the result, Woodhouse P. and Ongley J. held that the Government had breached its duty of care to the plaintiffs. Cooke J. dissented on the basis that no breach of duty had been proved.

The implications of the *Meates* decision are far-reaching. As yet, however, there is no Canadian case which takes such a broad view. Indeed, in *Taran Furs (Mtl.) Inc.* v. *Canadian Imperial Bank of Commerce*,[99] the Newfoundland Supreme Court expressly held that *Hedley Byrne* could not be extended to undertakings of future action.[100]

---

[97] *Ibid.*, at 335.

[98] *Ibid.*, at 379.

[99] (1984), 145 A.P.R. 128 (Nfld. S.C.).

[100] *Mooney* v. *National Museums of Canada* (1983), 47 B.C.L.R. 306 (S.C.), however, provides some support for *Meates*.

In another context, however, there is a line of crisis favouring the imposition of liability in tort for nonfeasance.[101] These cases are different from those considered so far because they do not involve express undertakings by the defendant. They are cases where the parties are in some existing professional or business relationship and where, as a result of that relationship, it can be inferred that the defendant has made some undertaking as to his future conduct upon which undertaking the plaintiff has relied to his detriment.[102] The classic situation covered is where an insurance agent negligently allows an insurance policy to lapse. This is what happened in *Morash* v. *Lockhart & Ritchie Ltd.*[103] The defendant had been the plaintiff's insurance agent for 20 years. During that time, the defendant had issued fire insurance policies on the plaintiff's house for three-year terms. As each policy was about to expire, the defendant had automatically sent a renewal policy to the plaintiff with an invoice which the plaintiff had always paid. In 1974, changes were effected in the fire insurance business whereby insurers started issuing policies for one-year terms rather than for three. For some reason, the plaintiff's three-year policy was not renewed when it expired in September 1974 nor was the plaintiff notified that it would not be renewed. The plaintiff did not discover that he had no coverage until his house was destroyed by fire in March 1976.

The Court held that the defendant was liable for the loss sustained by the plaintiff. It said very little, however, as to the basis for the imposition of the duty of care in these circumstances. The majority pointed out that it was common knowledge that insurance agents made a practice of sending their clients policy renewals and that where, as here, such a practice had been adopted, it was only natural that clients should rely upon it. The majority said simply:

> [T]he standard of reasonable care called for in circumstances such as were disclosed in the instant case required the defendant to notify the plaintiff in some way that his policy was not being renewed and that the omission to do so constituted negligence on the part of the defendant.[104]

It also pointed out that this was "not a case where an insurance agent either expressly or impliedly has undertaken to provide insurance coverage at a client's request".[105] Ryan J.A., dissenting in part, stated:

> [T]he defendant by its past conduct created for itself a self-imposed duty in law to renew the plaintiff's policy, or at least to have advised the plaintiff that it had expired. The defendant should have foreseen the possible risk of loss by fire to the plaintiff as a result of its negligent breach of duty, a loss which, in fact, occurred.[106]

It is submitted that Ryan J.A. comes closer to suggesting the true basis for the imposition of the duty of care. By its conduct during the ongoing relation-

---

[101] See generally Smillie, *supra*, footnote 1 at 269-74; and Feldthusen, *supra*, footnote 1 at 163-75.

[102] In this way, I prefer the reasoning of Smillie to that of Feldthusen, though I do not believe that there is any significant difference between their respective views.

[103] (1978), 95 D.L.R. (3d) 647 (N.B.S.C. App. Div.). See also *Grove Service Ltd.* v. *Lenhart Agencies Ltd.* (1979), 10 C.C.L.T. 101 (B.C.S.C.).

[104] *Ibid.*, at 650.

[105] *Ibid.*, at 649.

[106] *Ibid.*, at 655.

ship between the parties, the defendant had impliedly promised to renew the plaintiff's policy or to warn the plaintiff that it would not be renewed and the plaintiff had relied on that implied promise as the defendant should have realized. The Court, however, agreed that the plaintiff should bear some responsibility for not checking his own insurance coverage for some 18 months; accordingly, the majority reduced the plaintiff's damages by some 75 *per cent.*[107]

Clearly, it will always be difficult for a court to find liability where no express undertaking has been given by the defendant. No undertaking was inferred, for example, in *Argy Trading Development Co. Ltd.* v. *Lapid Developments Ltd.*[108] In that case, the defendants in 1971 leased certain warehouse premises to the plaintiffs for six years. By the terms of the lease, the plaintiffs covenanted to keep the premises insured against loss or damage caused by fire. The defendants already had a block insurance policy covering, *inter alia,* the plaintiffs' premises and advised the plaintiffs that there was no need for them to obtain separate insurance. They told the plaintiffs that this block policy would last until January 1972 and that the plaintiffs would be billed for their proportionate share of the premium. The plaintiffs paid this bill. In January 1972, the defendants renewed the block policy for a further year, but never demanded any payment from the plaintiffs. The Bank of Scotland later acquired a controlling interest in the defendants. It did not renew the block policy in January 1973 nor did it notify the plaintiffs that coverage was being cancelled. A fire later destroyed the premises; the plaintiffs sued to recover the lost insurance proceeds.

The Court dismissed the plaintiffs' claim and went too far in suggesting that there could never be liability in such a set of circumstances. For the reasons given by Feldthusen,[109] however, the decision itself seems correct. The case is very similar in this regard to *Maxey* v. *Canada Permanent Trust Co.*[110] The defendants were not in the business of providing insurance coverage. The relationship between the parties did not really go beyond that of lessor and lessee. There was little by way of past dealings through which any undertaking on the part of the lessor could be inferred.

Defendant Is in a Contractual Relationship with a Third Party

The principle of tortious liability discussed so far in this paper has been carried further so as to strike at the doctrine of privity of contract. It has been held, for example, that a defendant, who is under contract to and working for one party to a transaction, can at the same time be held to have undertaken to perform a service for another party to the same transaction. If the defendant in such circumstances performs his undertaking negligently to the plaintiff's detriment, the plaintiff will have a cause of action in tort. The best example of liability being found in these circumstances is the decision of the British Col-

[107]Ryan J.A. would have reduced the plaintiff's damages by 50 *per cent.*

[108][1977] 1 W.L.R. 444 (Q.B.D.).

[109]*Supra,* footnote 1 at 170-71.

[110]*Supra,* footnotes 87 and 92.

umbia Court of Appeal in *Tracy* v. *Atkins*.[111] In that case, the defendant was a solicitor acting for the purchaser in a real estate transaction. He was held to owe a duty of care to the vendors, who were not legally represented, on the basis of the following finding:

> In the circumstances of this case the solicitor undertook to carry out all the conveyancing including work that would ordinarily be done by the vendor's solicitor, such as registration of the mortgage back. By undertaking to do so he placed himself in the position of dealing with the plaintiffs' interests at a time when he knew or ought to have known that the plaintiffs were or might be relying on him to protect those interests. In the circumstances of this case he placed himself in "a sufficient relationship of proximity" that he incurred a duty of care towards the plaintiffs.[112]

The defendant was held liable for breach of his duty of care.

It will be much more difficult, but not impossible, to establish any such undertaking where the plaintiff is represented by his own lawyer. In *Allied Finance and Investments Ltd.* v. *Haddow & Co.*,[113] for example, the New Zealand Court of Appeal held that the solicitor for a borrower owed a duty of care to the lending company which was itself legally represented. The plaintiff lent money to one Hill on the security of a yacht which the plaintiff understood that Hill was buying. Before the money was advanced, the plaintiff's solicitor sent to the defendant, Hill's solicitor, a memorandum of the terms of the contract and an instrument by way of security over the yacht for Hill to execute and asked him for a certificate. The defendant returned the security instrument signed by Hill and certified "that the Instrument by Way of Security is fully binding on Roger Kenneth Hill" and "on behalf of our client, there are not other charges whatsoever on the yacht". The loan was then made. In fact, to the knowledge of the defendant, the yacht was being purchased by a company in which Hill was interested; the money was not intended to be used to enable Hill himself to purchase any interest in it. The Court agreed that normally a duty of care would not be owed by one solicitor to the client of another because "each solicitor is entitled to expect that the other party will look to his own solicitor for advice and protection".[114] In this case, however, where the defendant solicitor gave a certificate to the plaintiff upon which he would naturally rely, there was every reason to impose a duty of care. The proximity between the parties was "as close as it could be, short of contract".[115]

The greatest attack on privity has come in cases where it cannot be said that the defendant has given any undertaking to the plaintiff at all, but where the defendant has given an undertaking to some third party to perform a service of which the plaintiff is a beneficiary.[116] On occasion the courts have been

[111] *Supra*, footnote 37. See also *Deyong* v. *Weeks* (1983), 25 Alta. L.R. (2d) 117 (Q.B.), rev'd (1984), 33 Alta. L.R. (2d) 338 (C.A.); and *Rempel* v. *Parks*, *supra*, footnote 54, at 704-705 *per* Lambert J.A.

[112] *Ibid.*, at 636.

[113] [1983] N.Z.L.R. 22 (C.A.). See Todd, *supra*, footnote 96.

[114] *Ibid.*, at 24 *per* Cooke J.

[115] *Id.*

[116] See Smillie, *supra*, footnote 1 at 274-79; and Feldthusen, *supra*, footnote 1 at 145-58.

prepared to recognize that the defendant owes the plaintiff a duty of care in such circumstances despite the fact that by doing so they are, arguably, allowing a third party to enforce a contract made for his benefit but to which he is not privy. Disappointed beneficiaries under a will have been the principal plaintiffs in cases of this kind.[117] The typical situation arises where a solicitor, through his negligence, fails to ensure that the testator's wishes are effectuated, with the result that a gift under a will fails. It has been held that, in such circumstances, the disappointed beneficiary has a cause of action in tort against the negligent solicitor.

The Canadian example of this jurisdiction is *Whittingham* v. *Crease & Co.*,[118] where a gift to the plaintiff failed because the defendant negligently insisted that the plaintiff's wife witness the will. Aikins J. rationalized the solicitor's liability to the frustrated beneficiary on the basis of *Hedley Byrne*. The defendant had impliedly represented to the plaintiff that the will would be legally effective if his directions were followed. The plaintiff, who was present at the time of the execution of the will and who knew that he was the principal beneficiary under it, had passively relied on the defendant to see that the will was properly executed. There was no need for the plaintiff to establish any active reliance on the implied representation because the solicitor's negligence had caused the loss without there having to be any act on the part of the plaintiff to complete the chain of causation.

In the important case of *Ross* v. *Caunters*,[119] Megarry V.C. rejected the contrived reasoning of Aikins J. He pointed out that there was no need to fit this type of case within a narrow view of *Hedley Byrne*. There could be cases, such as *Ross* itself, where it would be impossible to speak of any reliance by the plaintiff because he would not know of any making of a will in his favour. Any decision, however, should not depend upon the fortuitous circumstances of the plaintiff's state of knowledge. The truth of the matter is that reliance is irrelevant in these cases. The defendant's undertaking is not made to the beneficiary. It is made to the testator. The plaintiff can recover because the undertaking is designed to benefit him. Megarry V.C. said:

> When a solicitor undertakes to a client to carry through a transaction which will confer a benefit on a third party, it seems to me that the duty to act with due care which binds the solicitor to his client is one which may readily be extended to the third party who is intended to benefit.[120]

If liability were not imposed in these circumstances, there would be little incentive for a solicitor to be careful in drafting and supervising the execution of a will.

---

[117] See the discussion of these cases in Smith, "Economic Loss and the Common Law Marriage of Contracts and Torts", *supra*, footnote 1 at 116-20; H. Luntz, "Solicitors' Liability to Third Parties" (1983), 3 *Oxford J. Leg. Studies* 284; and M.M. Litman and G.B. Robertson, "Solicitor's Liability for Failure to Substantiate Testamentary Capacity" (1984), 62 *Can. B. Rev.* 457 at 458-69.

[118] (1978), 88 D.L.R. (3d) 353 (B.C.S.C.).

[119] [1980] Ch. 297.

[120] *Ibid.*, at 309.

Ross v. *Caunters* was followed by the Supreme Court of Western Australia in *Watts* v. *Public Trustee for Western Australia*.[121] It was also applied by the New Zealand Court of Appeal in *Gartside* v. *Sheffield, Young & Ellis*[122] where it was alleged that the defendant solicitors had negligently delayed in drafting a new will for a testatrix with the result that she died in the interim. The trial judge had held that the statement of claim disclosed no cause of action.[123] He was clearly troubled by the effect that an acceptance of *Ross* would have upon the privity doctrine. The Court of Appeal, however, felt none of the concerns of the trial judge. It stressed the fact that the parties were in a highly proximate relationship. Richardson J., for example, pointed out: "[T]he designated beneficiary under the proposed will is so obviously and foreseeably likely to be closely and directly and adversely affected by any carelessness on the part of solicitor in that regard that the latter should have his interests in mind."[124] The Court also emphasized the fact that the absence of a remedy by the intended beneficiary could well mean that the solicitor would avoid any practical responsibility for his negligence, since the solicitor's client, the testator, has suffered no obvious loss. It was unaffected by the possibility that it was in some way eroding the doctrine of privity by granting a cause of action to a third party beneficiary under a contract. In any case, the Court did not see its decision as an infringement upon privity of contract. Richardson J. said:

> The contract of retainer between solicitor and client does not include any provision for the benefit of a third party. The benefit to the third party from the bounty of the client arises only when the contract is properly carried out. It is not conferred under the contract of retainer itself. The duty to the third party hinges on the existence of the contract of retainer but it is separate from the duty which the solicitor owes under the contract to this client ....[125]

Ross was, however, emphatically rejected by the Supreme Court of Victoria in *Seale* v. *Perry*.[126] In large part again, the Court was concerned with the effect that an acceptance of *Ross* would have upon the doctrine of privity of contract. It is worthwhile setting out Murphy J.'s consideration of this problem in full:

> Although the third party beneficiary clearly cannot sue for damages for breach of contract, because he has no rights springing from the contract, Megarry V.C. suggests that he can nonetheless sue for damages in tort for its negligent performance.
>
> He has a right, it is said, springing from the relationship between him and the negligent contracting party which is brought about or created by the contract. The duty-relationship to the third party is said to arise because the negligent contracting party knew that the other party to the contract intended to benefit the third party and, accordingly, he (the solicitor) owed the third party a duty to exercise reasonable care in the performance of the contract.

[121] [1980] W.A.R. 97 (S.C.).

[122] [1983] N.Z.L.R. 37 (C.A.).

[123] [1981] 2 N.Z.L.R. 547 (H.C.).

[124] *Supra*, footnote 122 at 47.

[125] *Ibid.*, at 49.

[126] [1982] V.R. 193 (S.C.). See P. Cane, "Negligent Solicitors and Doubly Disappointed Beneficiaires" (1983), 99 *L.Q. Rev.* 346.

> The cases mentioned above reaffirm the fundamental rule of the common law that the third party beneficiary cannot sue on the contract for damages or specific performance following a deliberate breach of or failure to perform a contract. It follows that the third party beneficiary cannot sue on the contract for damages or specific performance following a negligent breach of or failure to perform a contract.... It would appear that the submission that a duty is owed by a solicitor to a third party beneficiary in tort (and correspondingly that a right is enjoyed by a third party beneficiary in tort), a duty and right respectively arising solely because of the relationship created by or the work to be done under the contract, either runs counter to the fundamental rule or, surprisingly, avoids it. In my view it runs counter to it, for it asserts that rights may flow to a third party as a direct consequence of the contents of the contract, albeit a right in tort, and no rights are conferred on a third party by reason solely of the contract.[127]

In another context, the same concern with upholding privity of contract is evident in *Balsamo* v. *Medici*.[128] In that case a principal was prohibited from suing a sub-agent in tort for purely economic loss for negligently paying the proceeds of a sale to the wrong party, in part because such a suit would abrogate the concept of privity of contract. The Court held that it was not the law that a sub-agent was directly liable to the principal for all negligent breaches of his contract with the main agent. The principal's sole claim lay against the main agent who happened to be bankrupt. This conclusion was reached despite the fact that, if the main agent had sought contribution from the sub-agent, the sub-agent would have had no answer to that claim and the loss thus have fallen on the party who caused it.

Frustrated beneficiaries are not the only plaintiffs in cases of this kind. The principle is potentially very far-reaching. In this respect, *Hofstrand Farms Ltd.* v. *The Queen in Right of British Columbia*[129] is an important decision. The plaintiff had acquired the right to obtain Crown grants over certain Crown lands. He had entered into a contract to sell these lands as of December 31, 1976. He applied for the Crown grants in November 1976. They were issued in Victoria on December 29, 1976. They had to be registered in the Prince George Land Registry Office by the end of December for the sale transaction to be completed. The plaintiff persuaded a clerk in the Crown grant unit office to send the grants by the defendant courier. The defendant offered a one day delivery service. Through the defendant's negligence, the grants were delivered late; the plaintiff had to default on its contract of sale and suffered a loss of $77,000. The defendant had no knowledge of the contents of the envelope to be delivered and had never heard of the plaintiff.

A majority of the British Columbia Court of Appeal held that the defendant owed the plaintiff a duty of care which had been breached, and hence was liable to the plaintiff in the amount of $77,000. It determined that the courier owed the plaintiff a duty of care for three reasons. First, the Court looked at the nature of the service being provided. The defendant provided a one day delivery service. Such a service offers certainty and speed. When a lesser service is provided, the courier should be liable for its carelessness. Secondly, the

[127] *Ibid.*, at 209-210.

[128] [1984] 2 All E.R. 304 (Ch.D.).

[129] (1982), 131 D.L.R. (3d) 464 (B.C.C.A.).

Court looked at the nature of the communications usually sent by such a service. Such communications normally involved financial matter; so "it would be in the contemplation of a reasonable courier that if it was careless in performing this service, parties affected by the communication would suffer financial or other loss".[130] Finally, and most importantly, the Court pointed out that the Crown grant unit, if it had suffered loss as a result of late delivery, could have sued the courier for breach of contract. It would be unjust to deny relief to the other party to the communication simply because he was not in contract with the courier.[131]

The concept of privity of contract in itself should not be regarded as a barrier to imposing tortious liability in these sorts of situations. There is, however, a potential problem given that the real basis of the plaintiff's claim is that the defendant has performed improperly his contract with a third party. In that sense, the plaintiff's claim is a derivative one. It is submitted that, in the area of pure economic loss as opposed to physical damage, the plaintiff should stand in no better position in relation to the defendant than the third party who has a contract with the defendant.[132] If the defendant has protected himself from liability by his contract, then that protection should equally be available against the plaintiff in any action brought in tort. In *Hofstrand Farms* this problem was not addressed at all. It was, however, put forward in *Seale* v. *Perry*[133] as one of the difficulties with finding a solicitor liable to an intended beneficiary. It was also raised by Robert Goff L.J. in *Leigh & Sillavan Ltd.* v. *Aliakmon Shipping Co. Ltd.*[134] Commenting upon *Ross* v. *Caunters*,[135] Robert Goff L.J. said:

> To create the obviously hypothetical problem, let us imagine a testator asking a solicitor to prepare a will while on holiday together, and the solicitor, lacking his book of precedents, agreeing to do so as a matter of friendship but without assuming any legal responsibility. The will fails for some obvious defect in point of form. I cannot think that in such a case a disappointed legatee could sue the solicitor for damages. I ask myself why: and the answer must, I think, be that it is quite simply because, when C has a direct right of action in tort against A in respect of damages caused by A's breach of [his] duty to B, C's rights against A must be regulated by any provisions which controlled or limited B's rights against A.[136]

---

[130] *Ibid.*, at 477.

[131] It should be pointed out that the plaintiff was technically not the other party to the communication, but the Court reasonably treated him as the recipient of the package. See Feldthusen, *supra*, footnote 1 at 151-52. The decision of the British Columbia Court of Appeal was reversed by the Supreme Court of Canada (*sub. nom. B.D.C. Ltd.* v. *Hofstrand Farms Ltd.*) in a judgment rendered on 20 March 1986. The major basis for the Supreme Court's decision was that there was insufficient proximity between the parties because the courier had knowledge neither of the existence of the plaintiff nor of the existence of a class of persons whose interests depended upon timely transmission of the envelope. Moreover, it could not be said that the plaintiff had relied upon any undertaking made by the courier. Therefore, no duty of care was owed. The alternative ground for the decision was that, in any event, the loss suffered was too remote. Unfortunately, the Supreme Court did not deal with the peculiar problems raised by these third party cases and the fact that the plaintiff's claim was a derivative one.

[132] See Blom, *supra*, footnote 1 at 289-91.

[133] *Supra*, footnote 126 at 207 *per* Murphy J.

[134] [1985] 2 All E.R. 44 (C.A.). See Holyoak, "Economic Loss Revisited" (1985), 1 *P.N.* 94.

[135] *Supra*, footnote 119.

[136] *Supra*, footnote 134 at 76.

As a practical matter, a lawyer will be unable to exclude his liability for professional negligence; hence this particular problem is unlikely to arise in that context. The same cannot be said, however, of couriers and other potential defendants in this type of case. An argument can be made that the disappointed beneficiary cases should be regarded as unique. Apart altogether from any difficulties relating to exclusion clauses, there is the added factor that, if the intended beneficiary has no right of action, then the lawyer may escape liability entirely. Moreover, a major problem with cases like *Hofstrand Farms* is one of remoteness. Although the courier can foresee financial loss being suffered by those depending upon the communication, it may have no conception of the vastness of any potential economic losses.

Finally, it should be noted that there are cases which allow recovery by a person who is in no way a beneficiary of the defendant's contract with a third party.[137] In *Trident Construction Ltd.* v. *W.L. Wardrop & Associates Ltd.*,[138] for example, the plaintiff, a general contractor, had a contract with the City of Winnipeg for the construction of a sewage disposal plant. The City also had a contract with the defendant, Wardrop, to serve as the supervising engineer on the project. The Court held that Wardrop owed the plaintiff a duty of care with respect to its supervisory and design functions. Feldthusen[139] rightly supports the imposition of a duty of care in such cases because of the defendant's control over a contractor in these circumstances.[140]

Perhaps the most interesting of all the recent cases is *Fraser-Brace Maritimes Ltd.* v. *Central Mortgage and Housing Corp.*[141] This was not a case where the defendant's contractual undertaking to a third party was designed to benefit the plaintiff. It was a case where the defendant's failure to enforce another party's contractual obligations arguably caused the plaintiff to suffer economic loss. The defendant had a contract with Centennial for the construction of certain apartment buildings. Centennial had a contract with the plaintiff for the erection of the buildings. The terms of the contract between the defendant and Centennial provided that Centennial should supply a labour and material payment bond or some other security. The contract also provided that, where no bond had been furnished, progress payments would only equal 90 *per cent* of the value of the work done. Centennial did not provide a bond or other security and, moreover, the defendant paid Centennial 95 *per cent* of the value of the work done. Centennial encountered financial difficulties and failed to pay the plaintiff the full amount owing to it. The plaintiff sued the defendant for the economic loss resulting from what was alleged to be the defendant's negligent failure to enforce its contract with Centennial.

---

[137]See Feldthusen, *supra*, footnote 1 at 158-63.

[138][1979] 6 W.W.R. 481 (Man. Q.B.).

[139]*Supra*, footnote 1 at 159.

[140]See also the cases dealing with the liability of contractors, hired to reconstruct streets, for impeding access to merchants in the neighbourhood. These cases are discussed by Feldthusen, *supra*, footnote 1 at 161-63. Liability was imposed in such circumstances in *Trappa Holdings Ltd.* v. *District of Surrey* (1978), 95 D.L.R. (3d) 107 (B.C.S.C.).

[141](1980), 117 D.L.R. (3d) 312 (N.S.S.C. App. Div.).

The Court held that no duty of care was owed in these circumstances. It was clearly troubled by the doctrine of privity. Jones J.A. said that in effect the plaintiff was attempting to enforce the provisions of a contract to which it was not a party. The imposition of a duty in tort would be a direct entrenchment on the sphere on contract. Apart from these general invocations to the purity of privity, Jones J.A. also made the good point that "[t]he acceptance of the appellant's contention would unduly restrict the right of parties to contract and place an undue burden on them to protect the interests of third parties".[142] The plaintiff's sole rights should be based on its own contract with Centennial. By that contract, the plaintiff should have protected itself as much as possible. Indeed, there was evidence that the plaintiff was not aware of the provisions of the contract between the defendant and Centennial when it signed its own contract with Centennial.

NEGLIGENT PRODUCTION OF A DEFECTIVE CHATTEL OR BUILDING[143]

Traditional Position — No Recovery in Tort for Purely Economic Loss

Where a plaintiff has acquired, through a contract with a third person, a defective chattel or building which has been negligently produced by the defendant, the traditional position is clear: the plaintiff is unable to recover from the defendant purely economic loss whether direct, namely the cost of repairing the defective product, or consequential, such as loss of profits incurred while the product is being repaired. The plaintiff can succeed in tort only where the product has caused him personal injuries or has damaged some other property owned by him.

The leading case in this context is the decision of the Supreme Court of Canada in *Rivtow Marine Ltd.* v. *Washington Iron Works.*[144] For its logging operations, the plaintiff chartered a barge fitted with a crane designed and manufactured by Washington Iron Works and distributed by Walkem Machinery & Equipment Ltd. The crane had been negligently designed and manufactured by Washington with the result that it was likely to collapse at any time. Washington and Walkem became aware of the crane's defects and of the dangers they posed, but they neglected to warn the plaintiff. The plaintiff learned of the crane's defects after a similar crane had collapsed and killed its operator. The plaintiff immediately took the crane out of service to have it repaired. The plaintiff suffered a greater loss of profits than it would have if it had been warned immediately, because it was forced to remove the crane at the

[142] *Ibid.*, at 331.

[143] Many useful paper have been written on the topic of liability for products causing purely economic loss. See *e.g.* J.A. Smillie, "Liability of Builders, Manufacturers and Vendors for Negligence" (1978), 8 *N.Z.U.L. Rev.* 109; S. Schwartz, "Jurisprudential Developments in Manufacturers' Liability for Defective Products Where the Only Damage is Economic Loss" (1979-80), 4 *Can. Bus. L.J.* 164; P.F. Cane, "Physical Loss, Economic Loss and Products Liability" (1979), 95 *L.Q. Rev.* 117; Annis, *supra*, footnote 58; Smith, "Economic Loss and the Common Law Marriage of Contracts and Torts", *supra*, footnote 1; A. Grubb, "A Case for Recognizing Economic Loss in Defective Building Cases", [1984] *Camb. L.J.* 111; and Feldthusen, *supra*, footnote 1 at 177-208.

[144] *Supra*, footnote 44. In *Condominium Plan 782-1326 (Owners)* v. *Jodoin Developments Ltd.* (1984), 30 Alta. L.R. (2d) 388 (Q.B.), MacNaughton J. said that products which had been constructed rather than manufactured did not fall within the *Rivtow* decision. There seems to be no logical basis for any such distinction.

height of the logging season. The plaintiff, *inter alia*, sued the manufacturer for all of its loss of profits and for the cost of repairs.

The majority of the Court under Ritchie J. was in no doubt that the plaintiff could not recover these losses on the basis of the tort of negligent manufacturing. The crane had not caused personal injuries or any property damage. Such liability as was sought to be imposed was said to be contractual in origin and hence could not be enforced by a stranger to the contract. The plaintiff, in effect, was arguing that the crane was not of the quality it had a right to expect and it could not look to the law of tort to satisfy those expectations. Any relief by a consumer for defects in goods purchased and for consequential economic losses must lie in contract against the supplier and not in tort against the remote manufacturer. Having dismissed the plaintiff's claim for damages for negligent manufacturing, however, the majority did still grant a large measure of relief to the plaintiff. It held that once the manufacturer, and indeed the distributor, became aware of the dangerous nature of the crane, it was under a duty to warn the plaintiff of the danger. If the manufacturer had issued a timely warning, the plaintiff could have repaired the crane during the slack season. For breach of its duty to warn, therefore, the manufacturer was held liable for the additional loss of profits caused by having to take the crane out of action during the busy season. The ordinary loss of profits and the cost of repairs could not be recovered on that basis because those losses would have been incurred in any event. They would have been recoverable only if the manufacturer had been liable for negligent manufacturing; the majority refused to impose any such liability upon a manufacturer in respect of purely economic losses. The strict view propounded by the majority in *Rivtow Maine* has been followed on numerous occasions.[145] It, therefore, retains a strong hold upon the Canadian judicial conscience, although attempts have been made to distinguish it in particular situations.[146]

An Attack on the Traditional Position — Tortious Liability in Respect of Dangerous Defects

Despite the comparative youth of the decision in *Rivtow Marine*, there are now increasing signs that the principle represented by that case is on the defensive, particularly in situations, of which *Rivtow Marine* itself was an example, where the chattel or building in question is not merely defective but dangerous. The seeds for *Rivtow Marine's* destruction were contained in the case itself in the form of Laskin J.'s dissent. Laskin J. refused to find the manufacturer liable only on the basis of its failure to warn. He argued that, since a manufacturer was liable for physical damage caused by its defective products, it should also be liable for costs incurred to render a dangerous product safe. He said:

[145] *E.g.*, *Ital-Canadian Investments Ltd.* v. *North Shore Plumbing & Heating Co. Ltd.*, [1978] 4 W.W.R. 289 (B.C.S.C.); *Langille* v. *Scotia Gold Co-operative Ltd.* (1978), 33 N.S.R. (2d) 157 (S.C.); *Province of New Brunswick* v. *J.W. Bird & Co. Ltd.* (1981), 34 N.B.R. (2d) 593 (C.A.); *Owners: Condominium Plan Number 7821918* v. *Alldritt Development Ltd.* (1982), 24 Alta. L.R. (2d) 178 (Q.B.; and *Buthmann* v. *Balzer*, [1983] 4 W.W.R. 695 (Alta. Q.B.).

[146] *E.g.*, *Dominion Chain Co. Ltd.* v. *Eastern Construction Ltd.*, *supra*, footnote 9; *Canadian Western Natural Gas Co. Ltd.* v. *Pathfinder Surveys Ltd.*, *supra*, footnote 39; *Nielson* v. *City of Kamloops*, [1982] 1 W.W.R. 461 (B.C.C.A.); aff'd *sub nom. Kamloops* v. *Nielsen*, [1984] 5 W.W.R. 1 (S.C.C.); and *Robert Simpson Co. Ltd.* v. *Foundation Co. of Canada Ltd.* (1981), 34 O.R. (2d) 1 (H.C.); rev'd in part (1982), 36 O.R. (2d) 97 (C.A.).

> If physical harm had resulted, whether personal injury or damage to property (other than to the crane itself), Washington's liability to the person affected, under its anterior duty as a designer and manufacturer of a negligently produced crane, would not be open to question. Should it then be any less liable for the direct economic loss to the appellant resulting from the faulty crane merely because the likelihood of physical harm, either by way of personal injury to a third person or property damage to the appellant, was averted by the withdrawal of the crane from service so that it could be repaired?[147]

He pointed out that the same rationale which supports a manufacturer's liability for actual physical harm must also embrace "threatened physical harm from a negligently-designed and manufactured product resulting in economic loss".[148] This was not a case of a product which provided to be merely unmerchantable and, therefore, an appropriate case for the law of contract. It was a case where the product was dangerous. He would, therefore, have allowed the plaintiff to recover the full loss of profits suffered while the crane was being repaired,[149] as having been incurred in a successful attempt to avert any physical harm. He would also have allowed the plaintiff to recover the cost of repairs since that cost was incurred to mitigate the damage which would have been caused if the crane had been allowed to collapse.

The approach taken by Laskin J. makes sense.[150] A manufacturer's liability should not depend upon the fortuitous circumstance of whether its product actually causes injury. Indeed, the majority in *Rivtow Marine* in its creation of a duty to warn, exhibited a similar concern for imposing liability in respect of dangerous products. The judicial desire to control dangerous products is also illustrated by some lower court decisions which have allowed recovery for damage to the product itself caused by an accident.[151] The best example is *Chabot* v. *Ford Motor Co. of Canada Ltd.*[152] The plaintiff bought a truck from a dealer. The truck was later destroyed by a fire caused by a defectively installed drain plug in the oil pan. The Court held that the manufacturer was liable in tort for the loss of the truck. It distingished *Rivtow Marine* on the ground that the plaintiff was not claiming damages for the cost of repairing the defective part of the truck, nor was he claiming economic loss resulting from carrying out such repairs. He was seeking compensation for damage done to his truck in an accident caused by the defect.

The principle underlying Laskin J.'s judgment has been most often employed in the area of liability for defective buildings. In *Dutton* v. *Bognor Regis U.D.C.*,[153] a builder developed a housing estate on his own land. The foundations of the house in question were approved by the defendant council and then covered. The house was eventually purchased by the plaintiff.

[147] *Supra*, footnote 44 at 548-49.

[148] *Ibid.*, at 552.

[149] Laskin J.'s judgment is a little confusing on this point. He seems to award the plaintiff only its additional loss of profits, but such a conclusion cannot possibly stand with Laskin J.'s own reasoning.

[150] It was actually applied in *Fuller* v. *Ford Motor Co. of Canada Ltd.* (1978), 22 O.R. (2d) 764 (Co. Ct.).

[151] This is the position in a number of American jurisdictions. See Feldthusen, *supra*, footnote 1 at 181.

[152] (1982), 138 D.L.R. (3d) 417 (Ont. H.C.).

[153] *Supra*, footnote 6.

Serious defects then appeared in the structure of the house. It was found that the house had unsound foundations because it had been built on an old rubbish tip. The plaintiff's action against the builder was settled; the case centred on the liability of the defendant council. Lord Denning M.R. and Sachs L.J. thought that it would be anomalous for the council to be liable if the builder were not.[154] They, therefore, discussed a builder's liability in these circumstances. They both determined that the cracking in the house constituted physical damage.[155] This is a difficult proposition to accept in light of the general view that, to constitute physical damage, there must be some damage to property other than the manufactured product itself. Lord Denning M.R.'s view that physical damage had been caused, however, seems to have been based on the fact that the property constituted a danger and that damages should be awarded for the cost of rendering the house safe.

Stamp L.J. was of the view that the plaintiff's claim was one for purely economic loss and, as such, could not be successful. He said:

> Nor can I see any valid distinction between the case of a builder who carelessly builds a house which, though not a source of danger to person or property, nevertheless, owing to a concealed defect in its foundations, starts to settle and crack and becomes valueless, and the case of a manufacturer who carelessly manufacturers an article, which thought not a source of danger to a subsequent owner or to his other property, nevertheless owing to a hidden defect quickly disintegrates. To hold that either the builder or the manufacturer was liable except in contract would be to open up a new field of liability the extent of which could not, I think, be logically controlled....[156]

He was relieved from considering further the builder's liability because the builder was not a party to the action. Stamp L.J.'s views, however, were clearly echoed by the majority in *Rivtow Marine*. It is a pity that Stamp L.J. did not carry his reasoning to its logical conclusion. He pointed out that the reason why a distinction is drawn between the situation where a dangerous product causes damage and where a product is merely defective lies in the character of the duty. He said that there is "a duty not carelessly to put out a dangerous thing which may cause damage to one who may purchase it; but the duty does not extend to putting out carelessly a defective or useless or valueless thing".[157] It is submitted that this reasoning should allow a plaintiff to recover for the cost of repairing a dangerous product before it causes damage and for economic loss consequent thereon.

The subsequent decision of the House of Lords in *Anns* v. *London Borough of Merton*[158] also dealt primarily with the liability of a local authority on similar facts. Again, however, the Court considered the position of the

[154]It is submitted that it is not necessarily anomalous for a local authority to be found liable in tort and for the builder to escape liability. As was pointed out by Wilson J. in *Kamloops* v. *Nielsen, supra,* footnote 146, in the case of the tortious liability of the local authority there is no danger of tort law impinging on contract in any way. The rationale underlying *Rivtow Marine* can have no application in such a case. See also Blom, *supra*, footnote 1 at 296-97.

[155]*Supra,* footnote 6 at 396 *per* Lord Denning M.R. and 403 *per* Sachs L.J.

[156]*Ibid.*, at 414.

[157]*Ibid.*, at 415.

[158]*Supra,* footnote 6.

builder and came to much the same conclusion as that reached by Lord Denning M.R. in *Dutton*. Lord Wilberforce also characterized the damage to the property as physical damage but he also stressed that "what is recoverable is the amount of expenditure necessary to restore the dwelling to a condition in which it is no longer a danger to the health or safety" of the occupant,[159] relying on Laskin J.'s dissenting judgment in *Rivtow Marine*. It is submitted that not only did the cracks in the dwelling not constitute physical damage in the accepted sense but that liability should be imposed in respect of a dangerous building whether or not there are any physical manifestations of its defective state.

The builder's liability was directly considered for the first time in *Batty* v. *Metropolitan Property Realizations Ltd.*[160] In that case, the plaintiff took from the first defendant, a development company, a 999-year lease on a house built by the second defendant on the side of a hill. Some three years later, there was a severe slip of the natural strata of the hillside which damaged the garden. The evidence was that the house itself was doomed to slide down the hill some time within the next ten years because the subsoil on which it had been built was totally unsuitable. The house was, therefore, unsaleable. The Court held that the builder was liable in negligence for the plaintiff's loss. It doubted whether physical damage to the property was required. On the basis of *Anns*, it held that it was sufficient that there was an imminent danger to the health and safety of the occupants.[161] It had no hesitation in characterizing the risk as imminent even though the house might have survived for a further ten years.

This trio of English cases, therefore, lends support to the view that a manufacturer or builder should be liable in tort for the economic loss suffered in order to avert the threat of physical damage posed by a negligently produced chattel or building. The classification of the damage in two of these cases as physical damage seems to have been merely an attempt by the courts to obscure the fact that they were in reality granting relief for purely economic loss, in the belief that their decisions would not otherwise be acceptable. It is worth noting, however, that the House of Lords in *Pirelli General Cable Works Ltd.* v. *Oscar Faber and Partners*[162] clearly believed that the basis for any action in tort in these situations lay in the fact that physical damage had been caused to the building rather than in any notion that the building was dangerous.[163]

This trilogy has some support in Canada[164] and in the rest of the Commonwealth. Indeed, in New Zealand, these cases have been extended in the same way as suggested in *Pirelli* so as to come close to allowing recovery in

[159] *Ibid.*, at 505.

[160] *Supra*, footnote 53.

[161] *Ibid.*, at 571-72 *per* Megaw L.J.

[162] [1983] 2 A.C. 1.

[163] See Grubb, *supra*, footnote 143 at 115-18.

[164] *E.g.*, *Ordog* v. *District of Mission*, *supra*, footnote 63; and *Thompson* v. *Plainsman Development Ltd.*, *supra*, footnote 62.

respect of buildings which are defective but not necessarily dangerous. In *Bowen* v. *Paramount Builders (Hamilton) Ltd.*,[165] for example, Richmond P. said that it was sufficient to ground liability that the defect had caused or was threatening to cause physical harm to the structure itself rather than to the occupants or some external property.[166] It must be admitted, however, that he did also stress that "the courts would not be justifed in imposing a duty of care on builders tantamount to the full warranties normally implied in a building contract".[167] Cooke J. went even further. He held first that the loss in the case was not purely economic because the building had been damaged. He then said that he could not see "why the law of tort should necessarily stop short of recognizing a duty not to put out a carelessly defective thing, nor any reason compelling the courts to withhold relief in tort from a plaintiff misled by the appearance of the thing into paying too much for it".[168] In the later case of *Mount Albert Borough Council* v. *Johnson*,[169] Cooke J. expressly said that imminent danger to personal safety was not required to ground liability. A purchaser could recover in tort against a builder for "economic loss caused by negligence, at least when the loss is associated with physical damage."[170]

Tortious Liability in Respect of Non-Dangerous Defects

It has been seen that some of the negligent building cases have come very close to allowing a plaintiff to recover in tort against a builder simply because the building is worth less than the plaintiff had the right to expect under this contract with his vendor. These cases have thus trodden heavily upon contract's traditional domain. There are also cases dealing with the manufacture of chattels which have misinterpreted *Rivtow Marine* in such a way as to allow a consumer recovery from a manufacturer of purely economic loss.[171]

All such cases, however, must now be read in light of the recent decision of the House of Lords in *Junior Books Ltd.* v. *Veitchi Co. Ltd.*[172] This case

[165][1977] 1 N.Z.L.R. 394 (C.A.).

[166]*Ibid.*, at 410.

[167]*Ibid.*, at 413.

[168]*Ibid.*, at 423.

[169][1979] 2 N.Z.L.R. 234 (C.A.).

[170]*Ibid.*, at 239.

[171]*E.g.*, *Maughan* v. *Internatinal Harvester Co. of Canada Ltd.* (1980), 38 N.S.R. (2d) 101 (S.C. App. Div.); and *Associated Siding Applicators Ltd.* v. *Jonasson (E.S.) Contractors Ltd.* (1985), 57 A.R. 136 (Q.B.).

[172]*Supra*, footnote 7. See A.J.E. Jaffey, "Sub-Contractors — Privity and Negligence", [1983] *Camb. L.J.* 37; S.M. Waddams, "Tort Liability for Economic Loss: *Junior Books Ltd.* v. *Veitchi Co. Ltd.*" (1983), 8 *Can. Bus. L.J.* 101; S. Todd, "Fitness Duties in Tort" (1983), 10 *N.Z.U.L. Rev.* 273; and J. Blom, *supra*, footnote 1. In two recent decisions the Supreme Court of Canada has said expressly that the effect of *Junior Books* and, in particular, its impact on *Rivtow Marine* must await consideration for another day: see *Attorney-General for Ontario* v. *Fatehi* (1984), 56 N.R. 62 and *Kamloops* v. *Nielsen*, *supra*, footnote 146. In *Kamloops* the Supreme Court did indeed award damages in tort for purely economic loss. The case, however, did not concern the liability of a manufacturer or builder for negligent production but rather the liability of a local authority for negligence in the exercise of its statutory powers relating to the construction of buildings. Thus the local authority was not a link in a chain of contractual relationships; there was no danger that the imposition of tortious liability would in any way subvert principles of contract law. *Rivtow Marine*, therefore, could properly be distinguished (see footnote 154, *supra*). As Wilson J. said, *supra*, footnote 146 at 45, in such a case, assuming a sufficient degree of proximity between the parties, economic loss should be recoverable if "as a matter of statutory interpretation it is a type of loss the statute intended to guard against."

has opened up the real possibility that a manufacturer may be found to owe a duty of care to a consumer for products that are defective but not dangerous in any way. The defendant, a specialist flooring contractor, was hired to lay a floor in a factory which was being erected for the plaintiff by a building company, the main contractor. There was no privity of contract between the plaintiff and the defenant. The plaintiff alleged that the floor was defective owing to the defendant's negligence and claimed the cost of replacing the floor and the economic losses consequent upon such replacement, namely the cost of removing the machinery while the new floor was being laid and loss of profits suffered during that time. The plaintiff did not allege that the state of the floor was dangerous in any way.

By a majority of four to one, the House of Lords held that the plaintiff's averments disclosed a good cause of action.[173] It is not entirely clear, however, how far the decision can be carried. Lord Fraser pointed out that the proximity between the parties was extremely close, "falling only just short of a direct contractual relationship".[174] This close proximity distinguished the case from "the case of producers of goods to be offered for sale to the public".[175] Lord Roskill agreed that the relationship between the parties was as close as could be envisaged short of privity of contract.[176] In determining that there was a sufficient degree of proximity between the parties, he relied on a number of facts, including the following: the defendant had been nominated as the flooring sub-contractor by the plaintiff's architect; the defendant was a flooring specialist; the plaintiff had relied on the defendant's skill and experience; and the defendant, as a nominated sub-contractor, must have known of the plaintiff's reliance on it. Lord Raskill also agreed that the concept of proximity involves some degree of reliance which would not easily be found as between a consumer and a manufacturer where the consumer's real reliance is on his immediate seller.

It is submitted that there are intractable problems with the decision in *Junior Books* and with any potential extension granting a consumer a direct right of action against a manufacturer for the negligent production of shoddy goods. In many ways, an article can be determined as defective only by reference to the terms of a contract. Lord Fraser made this point in *Junior Books*:

> [A] building constructed in fulfilment of a contract for a price of £100,000 might justly be regarded as defective, although the same building constructed in fulfilment of a contract for a price of £50,000 might not. Where a building is erected under a contract with a purchaser, then provided the building, or part of it, is not dangerous to persons or to other property and subject to the law against misrepresentation, I see no reason why the builder should not be free to make with the purchaser whatever contractual arrangements about the quality of the product the purchaser wishes. However jerry-built the product, the purchaser would not be entitled to

[173]On similar facts, but without considering *Junior Books*, a statement of claim was struck out as disclosing no cause of action in *Owners: Condominium Plan Number 7821918* v. *Alldritt Development Ltd.*, *supra*, footnote 145. Moreover, *Junior Books* was expressly rejected in *Buthmann* v. *Balzer*, *supra*, footnote 145.

[174]*Supra*, footnote 7 at 482.

[175]*Id.*

[176]*Ibid.*, at 491.

> damages from the builder if it came up to the contractual standard. I do not think a subsequent owner could be in any better position....[177]

The terms of the contract between the manufacturer and his purchaser should, therefore, be considered before any direct suit by the ultimate consumer can be allowed. The ultimate consumer should be in no better position than that occupied by the first purchaser from the manufacturer. Under the present law, however, it is difficult to see how any exclusion clause, for example, could be effective as against the consumer who is not privy to the contract between the manufacturer and the first purchaser. In *Twins Transport Ltd.* v. *Patrick & Brocklehurst*,[178] a sub-contractor sought to rely on an exclusion clause in his sub-contract as against the owner. The judge rejected the sub-contractor's argument that its liability to the owner could be no greater than its liability to the main contractor on the basis that the owner was not a party to that sub-contract and therefore could not be bound by that clause. He did not refer at all to Lord Fraser's *dicta* in *Junior Books*. He did intimate, however, that his conclusion might have been different if it could have been shown that the owner had consented to the exclusion clause in some way. In fact the judge held that the exclusion clause, as a matter of construction, was not even effective as against the main character; so strictly speaking, the issue of whether it could be available against the owner did not arise.

Equally, the consumer should be in no better position with respect to the manufacturer than he stands in relation to his own seller. If he has contracted out of some of his contractual rights, he should not be able to assert those rights against the manufacturer by means of an action in tort. Again, it is hard to see how such considerations could be brought into play in any direct action in tort. In *Southern Water Authority* v. *Carey*,[179] however, the Court held that a sub-contractor could rely on an exclusion clause in the main contract to protect himself in a suit by the owner. It said that the presence of the exclusion clause was a relevant factor in applying Lord Wilberforce's two-stage test for finding a duty of care in *Anns* v. *London Borough of Merton*[180]. Although *prima facie* the sub-contractor owed a duty of care to the owner given the degree of proximity between the parties, there was a consideration here which ought to negative that duty. In that respect, the Court[181] applied the following *dicta* of Lord Roskill in *Junior Books*:

> During the argument it was asked what the position would be in a case where there was a relevant exclusion clause in the main contract. My Lords, that question does not arise for decision in the instant appeal, but in principle I would venture the view that such a clause according to the manner in which it was worded might in some circumstances limit the duty of care just as in the *Hedley Byrne* case [[1963] 2 All E.R. 575, [1964] A.C. 465] the plaintiffs were ultimately defeated by the defendant's disclaimer of responsibility.[182]

---

[177] *Ibid.*, at 483.

[178] [1984] 25 Build. L.R. 70 as discussed by Parkinson, "Excluding Sub-Contractor's Liability" (1985), 1 *P.N.* 51.

[179] [1985] 2 All E.R. 1077 (Q.B.). See Parkinson, *ibid.*

[180] *Supra*, footnote 6.

[181] *Supra*, footnote 179 at 1086.

[182] *Supra*, footnote 7 at 494-95.

One difficulty with Lord Roskill's *dicta* is that normally the exclusion clause in the main contract will not purport to protect the sub-contractor; therefore the reliance on *Hedley Byrne* is misplaced.[183] In *Carey*, however, the clause did expressly purport to protect the sub-contractor.[184] The case, therefore, offers little assistance to a defendant where such a feature is lacking.

There is no good reason in the normal case, therefore, to allow a direct action in tort by a consumer against a manufacturer in respect of safe, but defective, products. Such reforms as are desirable are best achieved by legislation in the sales and consumer protection areas.[185] Feldthusen[186] points out that a direct action in tort against a producer for non-dangerous defects might be justifed in the area of real property because of the dearth of any statutory sales scheme in that context. To leave a purchaser with his contractual rights is likely to leave him with very little.

CONCLUSION

This paper has shown that contract law has traditionally played a significant role in courts' decisions to deny recovery in tort for purely economic loss, but that contract's influence has now been arrested and that the whole area is in the process of being re-thought. One result of this re-appraisal should be the recognition that there is a large area of tort law in which recovery should be allowed for purely economic loss and over which principles of contract law should hold no undue sway. In some situations, however, such as those exemplified by *Hofstrand Farms*[187] and *Junior Books*[188], the encroachment of tort law threatens to upset reasonable private allocations of risk. It is to be hoped that, in the future, principles of contract and tort law will operate more harmoniously.

[183]See Waddams, *supra*, footnote 172 at 105.

[184]In *Carey*, the Court refused to find privity of contract between the parties on the basis of *N.Z. Shipping Co. Ltd.* v. *A.M. Satterthwaite & Co. Ltd.*, [1975] A.C. 154 (P.C.) (N.Z.) because the sub-contractor had not authorized the main contractor to obtain such protection.

[185]*E.g.*, *The Consumer Products Warranties Act*, R.S.S. 1978, c. C-30 as amended. See also Report No. 38, Alberta Institute of Law Research and Reform, "The Uniform Sale of Goods Act" (October, 1982) 110-27, which proposes the institution of a system of extended warranties in sales law. See also, *Consumer Product Warrantee and Liability Act*, R.S.N.B., 1978, c. C-18.1.

[186]*Supra*, footnote 1 at 207.

[187]*Supra*, footnote 129.

[188]*Supra*, footnote 7.