Freedom's Just Another Word For Nothing Left To Lose
By Richard G. Meyer

Freedom of contract, especially in regard to allocating risks of loss and damages, is a hallmark of construction law. The Economic Loss Doctrine (ELD) is intended to enshrine the principle of voluntary risk allocation by prohibiting participants in construction projects from suing for their economic losses in the absence of a contractual relationship. Recent court decisions have broadly construed economic loss to include the cost of repair (Tennessee), damage to any part of a building under construction (Indiana, Hawaii and Utah), damage to reputation and a company's goodwill (Kentucky), loss of profits (Texas and Arizona) and additional financing costs (Ohio).

In disallowing a claim by an Owner against a Subcontractor for purely economic damages, the Ohio Supreme Court held that "parties to a commercial transaction should remain free to govern their own affairs." The Court noted that recovery for economic losses "remains the particular province of the law of contracts." Nevertheless, in that same recent opinion, the Court reaffirmed its position that one who "negligently supplies false information" will be held liable for the recipient's economic losses. This exception to ELD obviously creates a gaping hole in the defenses from liability of any architect, design engineer and other supplier of information in a construction project.

The negligent furnishing of false information is just one of the many recognized exceptions to ELD, and therefore to freedom of contract, in construction law litigation. In construction cases, the Ohio Supreme Court has recognized ELD exceptions for supplying erroneous information and generally for non-contractual relationships which are sufficiently close to "substitute for privity of contract." Last month, the Hamilton County Court of Appeals recognized an ELD exception for any conduct which a jury determines to be an intentional tort. The Kentucky Supreme Court recently recognized an ELD exception for a construction manager's alleged "negligent misrepresentation" in scheduling contractors.

These cases are representative of the "special relationship" principle gaining acceptance nationally. In a recent West Virginia case, the Court held that it was for the jury to determine whether a special relationship existed between the engineer providing subsurface data and a tunnel drilling subcontractor who incurred $436,000 in economic losses by relying on the purportedly erroneous data. In a 2008 opinion the Idaho Supreme Court reached the same conclusion regarding a claim by the Owner against a design professional with whom the Owner had no contractual relationship. And a 2007 Iowa court opinion rejected the design professional's liability disclaimers in its contract with the Owner, holding that a Contractor's claim for economic losses had to be submitted to a jury.

Other ELD exceptions adopted in recent construction cases include building code violations (Hawaii), malicious injury (Wisconsin), indemnification claims (Illinois), residential inspections (New Jersey), intentional misrepresentation (Pennsylvania), unfair prejudice and "unique circumstances" (Idaho), violation of a construction defects statute (Nevada), and the creation of or failure to prevent a dangerous condition (Maryland). Most if not all of these involve time-consuming trials, and often lengthy appeals, just to determine whether the ELD exception applies in the particular case.

Having knowledge of various exceptions to ELD, all participants in the construction process need to develop pre-construction strategies for assuring that all economic losses be borne by the party best positioned to avoid creating them in the first place.