CONSTRUCTION LAW LETTER

Volume 30 • Number 5 May/June 2014

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PURE ECONOMIC LOSS—THE ROAD TO DANGER

Introduction

Throughout the years, *Construction Law Letter* has often reported on cases dealing with the concept of recovery of pure economic loss by a wronged party from a negligent party. The following brief note is intended to provide some background to that line of cases.

Pure economic loss is loss suffered by a person, which is not accompanied by physical injury or property damage. The Supreme Court of Canada has outlined a number of categories in which such damages can be recovered. One of the categories that had a profound impact on construction law is the negligent supply of shoddy goods or structures. Pure economic loss resulting from such negligent supply can currently be recovered if the negligence resulted in real and substantial danger to the public. The Supreme Court also made it clear that it does not consider those categories to be closed. At present, there is conflicting case law across the country as to whether pure economic loss resulting from non-dangerous defects could form a new category of recovery, or whether the Supreme Court of Canada has precluded pure economic loss claims for negligence in the absence of a danger. The following note will very briefly trace the history of economic loss jurisdiction before addressing the conflicting case law on the danger requirement.

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Construction Law Letter is published six times a year by LexisNexis Canada Inc., 123 Commerce Valley Drive East, Suite 700, Markham, Ont., L3T 7W8, and is available by subscription only.

ISBN 0-433-40930-4 ISSN 433409304
ISBN 0-433-44380-4 (Print & PDF)
ISBN 0-433-44664-1 (PDF)

Subscription rates: $245
$345 (Print & PDF)

A (Very) Brief History of Economic Loss

The law of torts, as we know it today, was triggered by a single snail that somehow got into a bottle of ginger beer and began to decompose. Somebody bought that particular bottle from a store and gave it to the unfortunate woman who ended up drinking both the beer and the remains of the snail. She subsequently complained of shock and severe gastroenteritis and sued the manufacturer. The resulting lawsuit became known as *Donoghue v. Stevenson* [*Donoghue*]. Until this decision, courts had held that damages had to be an incident of contract. Consequently, as the law stood at that point in time, the manufacturer could not be held directly liable to the consumer without some kind of contract, direct or implied. In *Donoghue v. Stevenson*, the House of Lords decided that this should no longer be so and allowed the plaintiff's claim against the manufacturer of the ginger beer for personal injuries suffered from drinking a bottle of their beverage containing the snail's remains.

The next step was taken in *Dutton v. Bognor Regis Urban District Council*, where a municipal council was held liable for pure economic loss resulting from negligent inspection of a house. Lord Denning M.R. argued that it would be unreasonable to hold a council liable if a negligently inspected house collapsed and injured a person, but not if the home owner detected the defect and repaired it in time to prevent the collapse.

While *Donoghue* restricted recovery of damages to reasonably foreseeable physical damage (*i.e.*, bad digestion), 32 years later, the House of Lords allowed recovery of pure economic loss (*i.e.*, loss occurring independently of any physical damage to person or property) in a case of negligent misrepresentation. In *Hedley Byrne & Co. v. Heller & Partners Ltd*. [*Hedley Byrne*], the House of Lords held:

> If someone possessed of quite a special skill undertakes, quite irrespective of contract, to apply that skill for the assistance of another person who relies on such skill, a duty of care will arise… [if such] a person takes it on himself to give information or advice to, or allows his information or advice to be passed on to, another person who, as he knows or should know, will place reliance on it, then a duty of care will arise.

In Canada, the first major step expanding the traditional law of torts was taken by the Supreme Court of Canada in the 1974 decision of *Rivtow Marine Ltd. v. Washington Iron Works* [*Rivtow*]. In *Rivtow*, one of the defendants designed and built cranes. The plaintiff bought one of the cranes from a second defendant to use it on its barge. Another crane built by the first defendant crashed and killed its operator, upon which the plaintiff pulled its crane from service. Later, the plaintiff discovered latent defects. The first defendant knew about the defects and had failed to warn the plaintiff. The plaintiff claimed for damages resulting from the crane's downtime as well as repair costs. The Supreme Court held that the manufacturer was not liable in tort for the costs of repairing the crane itself nor for any economic loss that would have been sustained as a result of the need to effect repairs. Such liability, the court held, would amount to a warranty and should not be enforced against a stranger to the contract. The court did, however, allow the recovery of that part of the loss that was a direct result of the crane being out of service in the busiest season of use.

Back in England, in 1978, in *Anns v. London Borough of Merton* [*Anns*], Lord Wilberforce took the opportunity to set forth a now famous two-part test:

> [I]n order to establish that a duty of care arises in a particular situation, it is not necessary to bring the facts of that situation within those of previous situations in which a duty of care has been held to exist. Rather the question has to be approached in two stages. First, one has to ask whether, as between the alleged wrongdoer and the person who has suffered damage there is a sufficient relationship of proximity or neighbourhood such that, in the reasonable contemplation of the former, carelessness on his part might be likely to cause damage to the latter—in which case a prima facie duty of care arises. Secondly, if the first question is answered affirmatively, it is necessary to consider whether there are any considerations which ought to negative, or to reduce or limit the scope of the duty or the class of person to whom it is owed or the damages to which a breach of it may give rise.

The Supreme Court of Canada adopted this *Anns* test at its first opportunity, in the 1984 case of *Kamloops (City) v. Nielsen*, where the City was held liable for 25 per cent of the economic loss of a subsequent purchaser of a house because the City had failed to prevent construction and occupation of house with defective foundation in contravention of a by-law.

Subsequent to this decision, the House of Lords overruled their *Anns* decision in *Murphy v. Brentwood District Council* [*Murphy*]. The Lords, lamenting the absence of any coherent and logically based doctrine for avoiding unlimited liability, which absence was bound to "put the law of negligence into a state of confusion defying rational analysis", returned to *Donoghue* and the proposition that economic loss could only be recovered in negligence where there was physical damage or in the *Hedley Byrne* situation.

In 1992, in *Canadian National Railway Co. v. Norsk Pacific Steamship Co.*, the Supreme Court of Canada, facing the contradictory decisions, chose to stick to the *Anns* test and rejected *Murphy.* The court held that where Party A negligently damaged the property of Party B, which in turn caused pure economic loss to Party C, Party C could recover that loss from Party A. In that case, a barge towed by the defendant collided with a bridge owned by Public Works, which bridge was used mainly by the plaintiff railway. The railway recovered the cost of rerouting its trains from the defendant.

In a construction law context, the reality of this line of cases was felt in the landmark 1992 decision of the Supreme Court of Canada in *Winnipeg Condominium Corp. No. 36 v. Bird Construction Co.* [*Winnipeg Condominium*]. On the facts of that case, more than 15 years after substantial completion of a condominium tower block, several tons of stone cladding fell to the ground injuring neither person nor property. The condominium corporation, which took title to remove from the original owner, claimed for the prospective costs of repairing or replacing the entire exterior stone cladding

(*i.e.*, pure economic loss). By the time the action was commenced, the only defendant left in business was the unfortunate general contractor, Bird Construction. The Supreme Court of Canada held that the costs of repairing defects in a building, resulting from negligent planning and construction, were recoverable from the former general contractor in tort "where that building is found to contain defects resulting from that negligence which pose a real and substantial danger to the occupants", even though there was no contractual *nexus* between or among any of the parties, and the limitation periods in the contract between the general contractor and its defunct masonry subcontractor had long since expired.

The Danger Requirement

The Supreme Court in *Winnipeg Condominium* made it clear that its reason for allowing recovery of economic loss resulting from negligence was the real and substantial danger the negligence had created. Subsequent decisions have elaborated on the requirement of danger. The Alberta Court of Appeal, for example, in *Vargo v. Canmore (Town)*, discussed in Volume 29:6 of *Construction Law Letter*, held that a finding of liability on the *Winnipeg Condominium* line of cases does not require the danger to be imminent. That decision was in line with two other appellate cases, *Mariani v. Lemstra* in Ontario and *Roy v. Thiessen* in Saskatchewan.

There are diverging opinions in the courts throughout the country right now on whether the decision in *Winnipeg Condominium* has precluded recovery for pure economic loss resulting from the supply of a defective but non-dangerous structure. In 2009, in *Dominion Construction Co. v. 4405633 Manitoba Ltd.*, a Manitoba court granted summary judgment dismissing a fourth-party claim by an engineering firm against a contractor for deficiencies in a concrete floor, based on the fact that there was no basis in Canadian law for a claim for pure economic loss resulting from the supply of a defective structure that did not pose a danger.

The Nova Scotia Court of Appeal, in *Sable Offshore Energy Inc. v. Ameron International Corp.* [*Sable*], held that *Winnipeg Condominium* expressly left open the question of recovery for non-dangerous defects, and therefore held that a claim for pure economic loss resulting from non-dangerous defects was not sure to fail.

For a while, it looked as if Ontario courts had shut the door on damages for non-dangerous defects, but the Court of Appeal has recently reopened that door. In *Barwin v. IKO Industries Ltd*. [*Barwin*], the court held that while the materials in question were dangerous, the claim would not necessarily have failed even had they not been dangerous, but merely shoddy. In *Arora v. Whirlpool Canada LP* [*Arora*], on the other hand, the court refused to follow *Barwin* and *Sable* and held that the law in Ontario was clear that non-dangerous defects could not form the basis for claims for pure economic loss. The court was bound on this point by the earlier Divisional Court decision in *Ducharme v. Solarium de Paris Inc*. [*Ducharme*]. The Ontario Court of Appeal dismissed an appeal from *Arora*, but in doing so, disagreed with the Divisional Court that the law was clear on this point. The court in *Ducharme* had simply stated that based on *Winnipeg Condominium*, no liability could result from non-dangerous defects. The Court of Appeal held that *Winnipeg Condominium* did not stand for that proposition.

Arora was not a construction case, but a case where consumers sued for economic loss for faulty washing machines. It was agreed by all parties that the machines posed no danger to anyone. The Court of Appeal dismissed the action on the basis that to recognize tort liability for defective, non-dangerous consumer products would represent such a quantum leap that it was plain and obvious that the negligence claim could not succeed. For the time being, however, the question of what happens when a construction project results in non-dangerous defects remains unanswered.