

# TORT IN A CONTRACTUAL MATRIX<sup>©</sup>

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This article addresses one aspect of the interface between tort and contract: the way tort law is affected, whether by extending or contracting its reach, by the parties coming together against a contractual structure. Two basic situations are considered. The first concerns the effect of a contractual limitation clause on the tort liability of, or to, a third party such as a subcontractor's to the building owner. The second considers what effect to attribute to a plaintiff's failure to protect himself or herself in advance by contracting against the risk.

Cet article aborde un aspect de l'interaction entre la loi des délits et celle du contrat: la façon dont la loi des délits est influencée, soit en élargissant ou en contraignant sa portée, par la rencontre des parties dans le contexte d'une structure contractuelle. Deux situations fondamentales sont considérées. En premier lieu, il s'agit de l'effet d'une clause contractuelle limitative sur la responsabilité de, ou à, un tiers, tel que la responsabilité d'un sous-contractant au propriétaire de l'édifice. Deuxièmement, nous considérons quel effet attribuer à l'échec du plaignant de se protéger en avance en contractant contre le risque.

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## I. INTRODUCTION

Contract and tort intersect in different contexts, occasioning problems that do not yield to any simple and uniform solution. Often, the question is whether any perceived gap in contractual doctrine, such as the insistence on privity or consideration, should be filled by a tort remedy.<sup>1</sup> I propose to address a very different question: the way in

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<sup>1</sup> Thus the “disappointed legatee” is not germane to my present remit; nor are the “black hole” problems such as *Leigh & Silavan Ltd. v. Aliakmon Shipping Co.*, [1986] A.C. 785 (H.L.) [hereinafter *The Aliakmon*], rev'g [1985] Q.B. 350 (C.A.); *The Albazero* [1977] A.C. 774 (H.L.); and

which tort law has been affected, whether by extending or contracting its reach, by a “contractual matrix,”<sup>2</sup> by “the parties com[ing] together against a contractual structure.”<sup>3</sup> My role thus defined guards me against the possible charge of harbouring, as a tort lawyer, a preference for tort solutions at the intersection between contract and tort. Indeed, far from this being the case, my preference for the contract solution—for example, in overcoming the “privity gap”—is not only based on the argument that it would spare us collateral problems (such as the applicability of limitation clauses), but also on the conviction that the difficulty stems from a flaw in our contract law which can, and should, be more expeditiously remedied on its own terms than by resort to tort.<sup>4</sup>

Let me begin with a preliminary observation. It is no exaggeration to say that the tort law of the last twenty-five years has been virtually obsessed with the question of negligent economic loss. That exclusive focus has tended to obscure the fact that the defining element in many of these cases was the contractual matrix in which the loss occurred. In recent years, however, the contractual context has moved into the foreground of discussion. The fact that the situations most frequently involving economic loss have their counterpart also in cases of property damage only confirms my thesis. Thus, in one of the construction cases, concerning a claim by the owner against a subcontractor, the loss incurred was not the cost of repairing the defect, but damage to adjacent property.<sup>5</sup> Another somewhat similar recent case also involved damage to tangible property, when a bailee’s servants caused structural damage to a warehoused transformer.<sup>6</sup> In both cases, the question was whether the *prima facie* duty of *Donoghue v. Stevenson*<sup>7</sup>

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*Linden Gardens Trust v. Lenesta Sludge Disposals* [1994] A.C. 85 (H.L.) [hereinafter *Linden Gardens*], app’d in *Darlington Borough Council v. Wiltshier Northern Ltd.* [1995] 1 W.L.R. 68 (C.A.). From that viewpoint, see F. Reynolds, “Contract and Tort: The View from the Contract Side of the Fence” (1994) 5 *Cant. L. Rev.* 280.

<sup>2</sup> I take this term from the judgment of La Forest J. in *London Drugs Ltd. v. Kuehne & Nagel Int’l Ltd.*, [1992] 3 S.C.R. 299 at 327 [hereinafter *London Drugs*].

<sup>3</sup> See *Pacific Associates v. Baxter*, [1990] 1 Q.B. 993 at 1010 (C.A.), Purchas L.J. [hereinafter *Pacific Associates*] at 1010. See also J. Blom, “Interface between Tort and Contract,” in P.T. Burns & S.J. Lyons, eds., *Donoghue v. Stevenson and the Modern Law of Negligence: The Paisley Papers* (Vancouver: Continuing Legal Education Society of B.C., 1991) 139.

<sup>4</sup> I am thinking here of claims like those of a subsequent purchaser of a housing unit against a negligent builder for the cost of repairing the defect. Compare *Winnipeg Condominium Corp. v. Bird Construction* [1995] 1 S.C.R. 85; and *Bryan v. Moloney* (1995), 69 A.L.J.R. 375 (Tasmania S.C.).

<sup>5</sup> *Norwich City Council v. Harvey*, [1989] 1 W.L.R. 828 (C.A.) [hereinafter *Norwich City Council*].

<sup>6</sup> *London Drugs* *supra* note 2.

<sup>7</sup> [1932] A.C. 562 (H.L.) [hereinafter *Donoghue*].

was negated by the contractual matrix in which the relation between plaintiff and defendant originated.

As an introduction to these “contort”<sup>8</sup> problems, the basic “concurrency” question should first be briefly addressed. English law, in contrast to the French,<sup>9</sup> eventually took the view that a contractual obligation between the parties does not preclude the concurrence of a tort duty in the same respect, so that the injured party has the option to pursue either a contractual or a tortious remedy. Initially encountered mainly in relation to claims for personal injury and property damage, application of this principle has been greatly increased by the contemporaneous expansion of negligence liability for economic loss, especially in its application to professional services by accountants, bankers, and lawyers.<sup>10</sup> The motivation behind this development seems to have been to make procedural and other advantages of tort, such as contribution or a more favourable starting point for the period of limitation, available to the claimant. Moreover, it makes no sense to withhold these advantages from recipients of contractual, as opposed to gratuitous, services. But the tort duty is subject to contractual modifications, such as a lower standard of care or limitation of liability, in deference to the belief in the primacy of private ordering.<sup>11</sup> In short, the starting point for tort in a contractual matrix is, to borrow Peter Cane’s pithy axiom, that “contract trumps tort.”<sup>12</sup>

## II. LIMITATION CLAUSES

Much more complex is the “triangular” situation: the effect, if any, of a contract upon the possible tort remedy of or against an outsider. Following closely on the steps of *Donoghue*, the *Grant* case<sup>13</sup> taught that the days when a contract duty to A precluded a tort duty to B

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<sup>8</sup> The term was coined by G. Gilmore, *The Death of Contract* (Columbus: Ohio State University Press, 1974) at 90.

<sup>9</sup> See T. Weir, “Complex Liabilities” in *Int’l Enc. Comp. L.*, vol. 11, Torts (The Hague; Boston: M. Nijhoff, 1983) at 12:52.

<sup>10</sup> *Henderson v. Merrett Syndicates* [1995] 2 A.C. 145 (H.L.) [hereinafter *Henderson*]; *Mouat v. Clark Boyce*, [1992] 2 N.Z.L.R. 559 (C.A. Wellington); and *Central Trust Co. v. Rafuse*, [1986] 2 S.C.R. 147 [hereinafter *Central Trust*].

<sup>11</sup> See *Central Trust*, *supra* note 10; and *British Columbia Hydro and Power Authority. BG Checo Int’l*, [1993] 1 S.C.R. 12.

<sup>12</sup> *Tort Law and Economic Interests* (Oxford: Clarendon, 1991) [hereinafter *Tort Law*].

<sup>13</sup> *Grant v. Australian Knitting Mills Ltd.* [1936] A.C. 85 (P.C.) [hereinafter *Grant*].

in the same matter were gone. The manufacturer's contractual promise to the buyer regarding the quality of the product no longer pre-empts an obligation in tort to the ultimate consumer. Conversely, the buyer's contractual warranty claim against the retail seller does not preclude a tort claim against a negligent manufacturer. It is the universality of this principle, which was being questioned in the two above-mentioned cases, to which we must now turn.

In the construction cases, the building owner contracts with a head contractor for the work to be performed. A subcontractor causes damage or other loss to the structure, for which the owner is seeking recovery. Paradigmatically, the subcontractor is under contract with the head contractor, but not with the owner who suffered the loss. The reason that the owner does not address his or her complaint to the contractual partner, namely the head contractor, may be the latter's impecuniosity (or bankruptcy), a common feature in a lightweight industry. Most of the recent cases have categorically denied any duty of care between these parties on the ground that the loss is purely economic when the claim relates to a deficiency in the work done.<sup>14</sup> That generalization is foreign to my topic except to the extent that it may rest, in this context, on the residuary argument that the plaintiff could have planned in advance to shift the risk by contract. Here I am concerned more specifically with cases where the contract between the building owner and the head contractor,<sup>15</sup> or between the head and subcontractor,<sup>16</sup> purported to exclude or limit liability. This situation is by no means limited to claims for purely economic loss, but can also arise, as one case has already shown,<sup>17</sup> in relation to property damage—where, in other words, “duty” is *prima facie* governed by *Donoghue*, rather than by any overriding constraints against recovery for negligent economic loss.

Can the building owner sidestep such a limitation clause by suing the subcontractor in tort? It would be unrealistic to reject such a claim outright on the ground that there is no “proximity,” the currently fashionable touchstone of “duty,” between the parties. The employment

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<sup>14</sup> Based on *Murphy v. Brentwood District Council* [1991] 1 A.C. 398 (H.L.) [hereinafter *Murphy*], categorizing such loss as economic. Such cases include *Simaan General Contracting Co. v. Pilkington Glass Ltd.*, [1988] Q.B. 758 (C.A.) [hereinafter *Simaan*]; and *Greater Nottingham Co-operative Society Ltd. v. Cementation Piling and Foundations Ltd.*, [1989] Q.B. 71 (C.A.) [hereinafter *Greater Nottingham Co-op.*]. Compare *Henderson*, *supra* note 10.

<sup>15</sup> *Southern Water Authority. Carey*, [1985] 2 All E.R. 1077 (C.A.).

<sup>16</sup> *Norwich City Council*, *supra* note 5. The clause excluded all liability for fire.

<sup>17</sup> *Ibid.*

of subcontractors was clearly contemplated at the time of contracting, and the risk of their negligence and its effect on the owner's interests was obvious. But was it "just and reasonable" (to use another favoured test of duty) to subject the subcontractor to liability in circumstances that included the contractual background against which he or she had agreed to perform services? Negating a tort duty can be squared with conventional analysis as an illustration of the principle of voluntary assumption of risk: inasmuch as the owner had agreed with the head contractor to assume the risk of defective performance above the stipulated sum, the owner assumed the risk of loss from negligence on the part of the contractor and those whom the latter deputed to perform the work. If, instead, the limitation clause was in the contract between the head and subcontractor, it signified all the more the subcontractor's unwillingness to do the job otherwise than subject to the limitation. At any rate, if known to the owner, the latter's acquiescence can be deemed an acceptance of the terms under which alone the subcontractor is prepared to enter into a relationship defining his or her duty with the owner. This, in substance, was the reasoning of the Court of Appeal in *Norwich City Council*, when denying altogether the existence of any duty of care owed to the plaintiff.<sup>18</sup>

Where the clause purports, however, to limit rather than exclude liability, should a tort duty not be recognized subject to the limitation clause in the contract? This issue has baffled the judges. In one such instance, *The Aliakmon*,<sup>19</sup> where the consignee of cargo sued the shipowner who had contracted with the consignor subject to the Hague-Visby Rules,<sup>20</sup> Donaldson M.R. gave as his principal reason for denying a tort duty, and Oliver L.J. as an alternative reason, that a tort duty would be "original," not derivative, and as such could not be subject to the limitation clause in the bill of lading. Only Goff L.J. in the Court of Appeal was prepared to invoke the concept of "transferred loss," and

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<sup>18</sup> *Ibid.* A limitation or exemption clause in a contract between a bailee and sub-bailee will bind an owner of the goods who expressly or impliedly consented to the sub-bailment on such terms. This conclusion is based not on privity of contract but on the rule that a sub-bailee, on receipt, assumes the obligations of the bailee: *The Pioneer Container* [1994] 2 A.C. 324 (P.C.). All the same, Goff L.J.'s reasoning based on consent could as well have general application.

<sup>19</sup> *Supra* note 1.

<sup>20</sup> *Protocol to Amend the International Convention for the Unification of Certain Rules of Law Relating to Bills of Lading* (Brussels: 23 February 1968), Schedule to the *Carriage of Goods by Sea Act 1971* (U.K.), 1971, c. 19 [hereinafter Hague-Visby Rules].

thereby recognize a tort claim subject to the contractual limitation.<sup>21</sup> It comes as no surprise that this imaginative solution, following the German model of *Drittschadensliquidation*<sup>22</sup> was promptly quashed by Brandon L.J. in the House of Lords.<sup>23</sup> Whichever the alternative—whether a total denial of duty or a duty qualified by the limitation—its significance is linked to the view that the operation of tort law in the context of a planned transaction calls for a modification of the rules familiar in the “classic” non-consensual situations like the typical traffic accident.

Less problematic, no doubt, would be a contractual solution. This is preferred by American courts, on the basis of either assignment or third-party beneficiaries, for claims against subcontractors and similar claims.<sup>24</sup> It neatly disposes of the problem of limitation clauses by respecting the contractual allocation of benefits and burdens. While at present this solution is blocked for British courts by the rigidity of the privity doctrine, its adoption is strongly recommended in the academic literature.<sup>25</sup>

The other illustration of a tort duty modified by a contractual matrix comes from the important pronouncement of the Supreme Court

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<sup>21</sup> The same result had earlier been contemplated by Roskill L.J. in the controverted case of *Junior Books Ltd. v. Veitchi Co.*, [1983] 1 A.C. 520 at 546 (H.L.) [hereinafter *Junior Books*]. For a full explanation of *The Aliakmon*, *supra* note 1, see Reynolds, *supra* note 1. The precise problem in *The Aliakmon*—the position of a buyer whose seller retained title at the time of the damage—has since, with Goff L.J.’s blessing, been removed by giving the buyer a contractual right to sue under the *Carriage of Goods by Sea Act 1924* (U.K.), 1924, c. 50. See R. Bradgate & F. White, “The *Carriage of Goods By Sea Act 1924*” 56 *Mod. L. Rev.* 188.

<sup>22</sup> See B.S. Markesinis, “An Expanding Tort Law—The Price of A Rigid Contract Law” (1987) 103 *L.Q. Rev.* 354 at 387ff.

<sup>23</sup> See *The Aliakmon*, *supra* note 1 at 820.

<sup>24</sup> See W. Jones, “Economic Losses Caused by Construction Deficiencies: The Competing Regimes of Contract and Tort” (1991) 59 *Cin. L. Rev.* 1051 at 1077-1101; and M.A. Eisenberg, “Third-Party Beneficiaries” (1992) 92 *Colum. L. Rev.* 1358 at 1402-06. The tort solution is generally, though not uniformly, rejected on the ground that the loss is economic.

The Supreme Court of Canada affirmed an “obligation pour autrui” in Quebec law: *Demers v. Dufresne Engineering Co.* [1979] 1 S.C.R. 146. That is more doubtful in French law: see I. Wallace, *Construction Contracts* (London: Sweet & Maxwell, 1986) at 5.22-5.26. B.S. Markesinis, *A Comparative Introduction to the German Law of Tort*, 2d ed. (Oxford: Clarendon, 1990) adds that, “it has never been doubted in German law that the contractual debtor can oppose against the third party/plaintiff all defenses etc. he may have against the contractual creditor.”

<sup>25</sup> See B.S. Markesinis, “Eternal and Troublesome Triangles” (1990) 106 *L.Q. Rev.* 566; and D. Beyleveld & R. Brownsword, “Privity, Transitivity and Rationality” (1991) 54 *Mod. L. Rev.* 48. The French theory of “groupes de contrats” has, however, since been dismantled by the Cass. Ass. plén., 12 July 1991, D. 1991.549; 1993 ZEuP 592, in a return to the privity requirement of Art. 1165 C. civ.

of Canada in *London Drugs*.<sup>26</sup> The plaintiff had delivered a transformer to a warehouse company for storage under a standard form contract that stipulated a limitation of liability on any package to \$40. The transformer was severely damaged when two employees, while trying to move the transformer with forklift trucks, caused it to fall. Could the plaintiff circumvent the limitation clause by suing the employees in tort?

In contrast to the preceding cases against subcontractors who, presumably, were at least covered by liability insurance, permitting a claim against employees would seem at first glance particularly unfair, if not incongruous, with a modern understanding of labour relations. The cost of accidents, it is generally believed, is a charge on the employer, since the employer, unlike the employee, is able to plan against and absorb it as an overhead of the operations. Nor is it surprising that so few cases have raised the issue of the tort liability of employees, because they are rarely worth suing. It would only be in exceptional circumstances that employees have insurance of their own (for example, on their own cars), or otherwise command sufficient financial resources to satisfy a judgment. Thus, the argument that it would be unfair to deny the injured plaintiff redress against the guilty employee misses the target, since the plaintiff could not count on the employee's ability to answer for the damage. The rare case, such as perhaps *London Drugs*, where the employer's insurance policy also covered the employees, does not justify a contrary conclusion.

Likewise, from the employer's point of view, the employer cannot be expected to bail out the employee in the circumstances. The employer's contract with the owner of the transformer, limiting his liability to \$40, meant that it was up to the latter to procure extra insurance. It would thus upset the whole pattern of the warehouse agreement for the employer to be saddled with the cost of the accident.

Ultimately, limiting the employer's liability to \$40 would not defeat the plaintiff's expectations. Obviously, the warehouse contract envisaged the participation of employees, and it would be quite unrealistic to suppose that the plaintiff, while assuming the risk of loss in excess of \$40 *vis-à-vis* the warehouse operator, reserved recourse against the latter's employees. Indeed, the benefit of such a manoeuvre, were it to succeed, would enure not to the plaintiff, but to the insurer, who would be subrogated to his claim against the hapless employee. Thus, once again, the intendment of the whole planned arrangement would be

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<sup>26</sup> *Supra* note 2 at 299. See also the perceptive economic analysis by N. Siebrasse, "Third-Party Beneficiaries in the Supreme Court: Categorization and the Interpretation of Ambiguous Contracts" (1995) 45 U.T.L.J. 47.

frustrated, not only for the benefit of the tort victim, but for *his or her* insurer, who would gain a windfall by being enabled to shift to another party a loss which he had contracted to underwrite. From every functional point of view, then, the claim against the employees should fail, at least in excess of \$40, if not altogether.

And so it did. But how?<sup>27</sup> The majority adopted the contract approach by facing down the privity rule and allowing a limited *jus tertii* to the employees. They should be entitled to invoke a limitation clause in the contract between their employer and the plaintiff if: (1) that clause expressly or impliedly extends its benefits to employees seeking to rely on it; and (2) the employees acted in the course of their employment and in the performance of the very services provided for in the contract when the loss occurred. The remaining three justices preferred the tort approach. McLachlin J. expressed her unease, not so much with modification of the privity doctrine, as with the finding of the majority that the employees were implied beneficiaries of the limitation clause, although they had not been so much as mentioned in the contract. To give them the benefit of such a clause was to travel far beyond the so-called Himalaya clauses, which had eventually gained recognition by the Privy Council<sup>28</sup> and could most probably not have been accomplished even under statutes (such as New Zealand's *Contracts Privity Act 1982*<sup>29</sup>) giving the benefit of contract promises to "intended beneficiaries." She preferred the "duty" approach from the above-mentioned English cases. Essentially based on voluntary assumption of risk, it recognized that a duty of care can be waived or qualified in the light of the contractual matrix. By agreeing to the limitation clause, the customer had accepted that the risk of damage above \$40 in the performance of the contract was to be the customer's alone.<sup>30</sup>

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<sup>27</sup> For more extensive treatment, see J.G. Fleming, "Employee's Tort in a Contractual Matrix: New Approaches in Canada" (1993) 13 Oxford J. Legal Stud. 430. See also G. Huscroft & J. Manning, "Employee Liability in Tort: Closing the gap between principle and reality" [1993] N.Z. Recent L. Rev. 210.

<sup>28</sup> See *N.Z. Shipping Co. v. A.M. Satterthwaite & Co.* [1975] A.C. 154 (P.C.); *Port Jackson Stevedoring Pty. Ltd. v. Salmond & Spraggon (Australia) Pty. Ltd.* [1981] 1 W.L.R. 138 (P.C.); and *ITO-International Terminal Operators Ltd. v. Miida Electronics Inc.* [1986] 1 S.C.R. 752.

<sup>29</sup> 1982, N.Z. Stat. No. 132., as am. 1988, No. 110, ss. 10(2), 62, and 63; 1989, No. 107, s. 10(1); and 1991, No. 61, s. 19(1).

<sup>30</sup> A similar solution had been anticipated in *Norwich City Council*, *supra* note 5 at 833-34:

In addition, the plaintiff pointed to the position of the first defendant, the subcontractor's employee. Ex hypothesi he was careless and even if his employer be held to have owed no duty to the building owner, on what grounds can it be said that the employee himself owed no such duty? In my opinion, however, this particular point does not take the

The most drastic departure from orthodoxy was La Forest J.'s challenge to the putative liability of employees for torts committed in performing their employer's contractual obligations. In cases like the present, involving a planned transaction with the employer, the plaintiff can be considered to have chosen to deal with a company. The employees were not given to understand that the plaintiff was relying on them for compensation. Placing liability exclusively on the employer puts it on a party that is easily able to modify its exposure by contractual stipulation. In contrast, the employees had no real opportunity to decline the risk, nor could their union be expected to bargain over an issue that so rarely assumes practical significance. La Forest J. sympathized with the position adopted in several legal systems, including statutes in the Australian states of New South Wales, South Australia, and the Northern Territory, which have totally abrogated the tort liability of employees. However, he prudently confined his holding within the parameters of the case before him, to what he called "contractual vicarious liability"—that is, cases within a contractual matrix.

La Forest J.'s reasoning led him to dissent from the conclusion of the rest of the Court in that the defendants were liable, but only for breach of a "\$40 duty." His view of the employees' tort immunity, based on policy rather than derived from the contract itself, meant that the employees were not liable at all. In other words, they were not *pro hac vice* identified with their employer any more than with his contract. This conclusion more closely reflects the commonly held perception, reinforced by the public policy behind vicarious liability, that employees should not incur any liability for the torts committed by them in the course of employment, but should be subject merely to disciplinary sanction by their employer. On that view, the contractual setting should be irrelevant, in which case neither the majority's preference for a *jus quaesitum tertior* nor La Forest J.'s limitation of employees' tort immunity to a contractual context looks like the ideal long-term solution. The latter proves acceptable only as a step in the right direction.

Neither formula espoused in *London Drugs* would have defeated the plaintiff in the latest case of *Marc Rich & Co. A.G.v. Bishop Rock Marine Co.*<sup>31</sup> The defendants' vessel loaded the plaintiff's cargo under a

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matter very much further. If in principle the subcontractor owed no specific duty to the building owner in respect of damage by fire, then neither in my opinion can any of its employees have done so.

<sup>31</sup> [1994] 1 W.L.R. 1071 (C.A.) [hereinafter *Marc Rich*].

bill of lading limiting liability within the Hague Rules.<sup>32</sup> A surveyor employed by a classification society inspected the vessel and recommended that she continue on her voyage. Shortly after leaving port the vessel sank with loss of the plaintiff's cargo. The plaintiff, having settled with the shipowners for the contractual limit, sought to recover the remainder of the loss from the classification society. But the Court of Appeal dismissed the claim—for what was treated as a physical, not an economic, loss—denying a duty of care to the cargo owner primarily on the ground that, since the shipowners bore primary, contractual liability for the cargo under the complex international code of the Hague Rules, it was not fair, just, or reasonable to impose a virtually identical tort duty on the classification society without the same balancing factors contained in the Rules. Mann L.J. noted an affinity to *Norwich City Council*<sup>33</sup> and *Pacific Associates*<sup>34</sup> where a “contractual structure” had likewise negated a tort duty. He admitted, however, that, while relevant, the circumstances of these cases were different. The difference, surely, was that the classification society was not performing the contractual obligation of the shipowners, at least not in the same sense as the subcontractor and the engineer had done in the earlier cases. There clearly must be a closer nexus between the “contractual structure” and the defendant's obligation for the one to define the other. The decision of the Court of Appeal in *Marc Rich* has been affirmed by the House of Lords, though which did not advert to issues relevant to the present inquiry.<sup>35</sup>

### III. DEFENSIVE CONTRACTS

I come now to a second situation relevant to defining the scope of tort in the light of contract. A powerful argument, heard of late, purports to deny a duty of care, particularly a duty to avoid pure economic loss, if the claimant should have exercised his ability to guard against the risk by self-protective measures, such as by contract with the

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<sup>32</sup> International Conference in Maritime Law (Brussels, 1924) *Convention for the Unification of Certain Rules of Law Relating to Bills of Lading* (Dublin: Stationery Office, 1994), as set out in Schedule B to the *Carriage of Goods by Sea Act, 1924* (U.K.), 14 & 15 Geo. 5, c. 22 [hereinafter Hague Rules].

<sup>33</sup> *Supra* note 5.

<sup>34</sup> *Supra* note 3.

<sup>35</sup> [1995] 3 A.C. 227 (H.L.).

defendant or an intermediary. It was first voiced in *The Aliakmon*,<sup>36</sup> in support of the decision by the House of Lords to deny a tort remedy against a negligent carrier to a consignee to whom the risk, but not the property in the goods, had passed at the relevant time. Brandon L.J. offered the buyers the cold comfort that they should have either contracted with the sellers to exercise the right to sue the carrier, or assigned such a right to them.<sup>37</sup>

Brandon L.J.'s suggestion has struck a responsive chord in later cases. It has, for example, played a role in the construction area in denying tort recovery to a building owner against a subcontractor, or to a contractor against the owner's supervising engineer,<sup>38</sup> on the reasoning that the claimant could have contracted with the defendant for additional protection; indeed, the claimant's failure to do so implied an unwillingness to enter into formal relations with the defendant.<sup>39</sup> Thus, accountants have been absolved from liability to investors, and even to existing shareholders, on the ground, among others, that such plaintiffs should have procured independent advice.<sup>40</sup> This argument is also encountered in its negative form, namely, that the plaintiff's inability to plan against the contingency of loss favours recognition of a duty of care by the defendant. Hence the solicitor is liable in tort to the testator's intended beneficiary, where the latter's inability to guard against the loss reinforces the desirability of furnishing a sanction against professional negligence.<sup>41</sup> Also, in the remarkable decision of *Smith v. Bush*,<sup>42</sup> a mortgagee's valuer was exceptionally held liable to the purchaser of a "modest" home for an overvaluation, in view of the purchaser's

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<sup>36</sup> *Supra* note 1 at 819. See *Tort Law and Economic Interests*, *supra* note 12 at 345-48.

<sup>37</sup> But this advice stopped short of recognizing an equitable *duty* to sue on behalf of the consignee, perhaps in deference to an *obiter* remark by Diplock L.J. in *The Albazero*, *supra* note 1 at 845. Arguing in favour of such a duty is R.M. Goode, "Ownership and Obligation in Commercial Transactions" (1987) 103 L.Q. Rev. 433 at 453ff. On the measure of damages in a suit by the consignor, see *Gus Property Management v. Littlewoods Mail Order Stores Ltd.* [1982] S.L.T. 533 (H.L.); and *Linden Gardens*, *supra* note 1.

<sup>38</sup> See, for example, *Simaan*, *supra* note 14; and *Pacific Associates*, *supra* note 3. Compare *Invercargill City Council v. Hamlin*, [1994] 3 N.Z.L.R. 513 at 520 (C.A.), Cook P., who expressed the view that, in cases of "industrial construction, the network of contractual relationships normally provides sufficient avenues of redress."

<sup>39</sup> This is still more persuasive if there existed a contract between plaintiff and defendant that dealt with extraneous matters, as in *Greater Nottingham Co-op.*, *supra* note 14.

<sup>40</sup> *Caparo Industries PLC v. Dickman*, [1990] 2 A.C. 605 (H.L.).

<sup>41</sup> *White v. Jones*, [1995] 2 A.C. 207 (H.L.). See also B.S. Markesinis, "Five Days in the House of Lords" (1995) 3 Tort L. Rev. 169.

<sup>42</sup> [1990] 1 A.C. 831 (H.L.) [hereinafter *Smith*].

unfamiliarity with business matters which excused her failure to contract for independent advice as one would have expected from a business person.

Recently, my friend Jane Stapleton has repeatedly championed Brandon L.J.'s argument as part of a larger agenda to roll back the expansive pretensions of tort law during the Wilberforce era of the 1960s and 1970s by directing the duty focus, not exclusively to the defendant's, but equally toward the plaintiff's, conduct.<sup>43</sup> In the past, it had become fashionable, especially among academic tort enthusiasts, to approach new situations by asking, "Why not?," and the time had come to ask "Why?" instead. Not that the focus should be solely on a plaintiff's alternative means of self-protection; self-protection by first party insurance was especially not about to be recognized as an adequate means.<sup>44</sup> To qualify as adequate, the alternative means also had to present also an adequate opportunity to deter the defendant. This was so in the "contractual matrix" situations, where—to take *Pacific Associates*<sup>45</sup> as an illustration—the contractor was denied a remedy against the engineer because the contractual structure gave him an adequate remedy against his employer, the building owner, who in turn could subject the engineer to sanction and deterrence. Rather than rationalizing the decision, as the Court did, by refusing to allow the plaintiff to circumvent the "clear basis" of understanding between three commercial parties, a more objective criterion, less prone to slide into fiction, was to say that the plaintiff had a reasonable opportunity to deal directly with an intermediate party in a way that would exert deterrence incentives on the defendant. *Smith*,<sup>46</sup> by contrast, illustrates, not the facile distinction presented by a plaintiff of modest means, but a market condition which precluded negotiable variations at the modest end of the housing market.

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<sup>43</sup> Her thesis, that absence of opportunity for self-protection was a necessary (though not sufficient) condition of tort recovery, was first voiced in J. Stapleton, "Duty of Care and Economic Loss: A Wider Agenda" (1991) 107 L.Q. Rev. 249 [hereinafter "A Wider Agenda"]. It has since been refined by "adequate opportunities for deterrence," and is no longer restricted to claims for economic loss: see J. Stapleton, "In Restraint of Tort" in *The Frontiers of Liability* vol. 2 (Oxford: Oxford University Press, 1994); and J. Stapleton, "Duty of Care: Peripheral Parties and Alternative Opportunities for Deterrence" (1995) 111 L.Q. Rev. 301 [hereinafter "Alternative Opportunitites"].

<sup>44</sup> This is not a self-evident proposition. The mirror image of universal accident compensation is the replacement of all tort liability by first-party self-insurance, optional or mandatory. Intellectually, the one is as radical a departure from traditional concepts about accident compensation as the other. See "Alternative Opportunities," *supra* note 43.

<sup>45</sup> *Supra* note 3.

<sup>46</sup> *Supra* note 42.

Yet, despite its evident appeal, this thesis cannot be accepted without reservations. It not only lacks any consistent judicial support, but is also plainly incompatible with many leading decisions. Such, for example, is the pivotal precedent of *Hedley Byrne & Co. v. Heller & Partners Ltd.*<sup>47</sup> where the plaintiff, in Stapleton's terminology, clearly chose to "take a free ride" by relying on the banker's gratuitous advice concerning the credit of one of its customers. Also, in the important Canadian case of *Norsk*,<sup>48</sup> it was given short shrift in a true contractual matrix. In *Norsk*, the defendants, negligently navigating a barge, collided in heavy fog with a bridge owned and operated by a public authority. The plaintiffs, under licence from that authority, were the principal users of the bridge, and sued for their loss caused by the disruption of its use. A majority of the Supreme Court of Canada, casting aside prior English authority, allowed the tort claim against the bargees, notwithstanding the availability of contractual planning against that risk with their contractual partner, the owner of the bridge. Yet, as La Forest J. in his masterly dissent pointed out, the plaintiffs were in a much better position to assess that risk than were the defendants, and could easily have shifted it to the bridge owner in their contract with it.<sup>49</sup>

In *Edgeworth Construction v. N.D. Lea & Associates Ltd.*<sup>50</sup> a unanimous Supreme Court of Canada decided in favour of a contractor against an engineering firm for negligent specifications embodied in a provincial construction project. The Court held that the presence of an exclusion clause in the contract between the plaintiff and the province did not purport to limit any tort duty by the engineering firm. Even La Forest J. did not distance himself from the rest of the Court by drawing attention to the contractor's failure to protect himself either in his

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<sup>47</sup> [1964] A.C. 465 [hereinafter *Hedley Byrne*]. Not surprisingly, this has been belittled by Stapleton: "[F]ar from correcting a 'wrong turning,' *Hedley Byrne* judged by today's standards may have been one itself." See "A Wider Agenda," *supra* note 43 at 259.

<sup>48</sup> *Norsk Pacific Steamship Co. v. CNR*, [1992] 1 S.C.R. 1021 [hereinafter *Norsk*].

<sup>49</sup> In defence of La Forest J.'s dissent, see N. Siebrasse, "Economic Analysis of Economic Loss in the Supreme Court of Canada: Fault, Deterrence, and Channelling of Losses in *CNR v. Norsk Pacific Steamship Co.*" (1994) 20 Queen's L.J. 1.

<sup>50</sup> [1993] 3 S.C.R. 206 [hereinafter *Edgeworth Construction*]. This decision is clearly distanced from *Gran Gelato v. Richcliffe (Group) Ltd.*, [1992] Ch. 560, where Nicholls V.-C. denied a remedy against a seller's solicitor who had made a direct misrepresentation to the purchaser, on the ground that the latter had a contractual remedy against the vendor (who happened to be bankrupt). The decision has been castigated by P. Cane, "Negligent Solicitor Escapes Liability" (1992) 108 L.Q. Rev. 539. Compare *South Pacific Mfg. Co. v. New Zealand Security Consultants & Investigations Ltd.* [1992] 2 N.Z.L.R. 282 (C.A. Wellington) (disallowing a tort action against an investigator, employed by the plaintiff's insurance company, who had incriminated the plaintiff of arson).

contract with the province, or by contracting directly with the defendants.<sup>51</sup>

A final example is the even more recent House of Lords decision in *Henderson*,<sup>52</sup> from the aftermath of the Lloyd's of London disasters of the past decade. The so-called Indirect Names brought action for professional negligence, not only against their own members' agent, with whom they were in a contractual relation, but also against managing agents of syndicates with which risks were placed. Goff L.J. rejected the analogy of the string contract building cases by finding a clear case of assumption of responsibility towards the Names, sufficient for tort responsibility, notwithstanding their undoubted remedy, concurrently in contract and tort, against their own agent. Stapleton rightly rebukes Goff L.J. for resting his reasoning on the mere assertion of assumption of responsibility without an explanation of what it was about the structure of the contractual chain that differentiated this case from *Simaan*<sup>53</sup> and others. But, by the same token, does this not also throw doubt on the stability of the competing concept of "adequate opportunity for self protection?"<sup>54</sup> This concern centres poignantly on *Smith* with its stress on the purchase of the "modest dwelling" by a woman unfamiliar with business affairs. While that approach was entirely praiseworthy for its sensitivity to social realities—and corresponds with the distinction drawn by legislation in England between the rights of subsequent buyers of homes and those of subsequent buyers of commercial property against the original builder<sup>55</sup>—it is difficult to reconcile with Brandon L.J.'s insistence on observing a "clear bright line" in cases of economic loss.<sup>56</sup>

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<sup>51</sup> Another interesting aspect of the decision, germane to this article, was the acquittal of the individual engineers employed by the firm. Unlike in *London Drugs*, *supra* note 2, they were not intended beneficiaries of their employers' exemption clause. In the Court's view, however, the fact that they had affixed their seal to the design documents was insufficient to establish a duty of care to the plaintiff. As elaborated by La Forest J., the plaintiff did not rely on them, but on their firm's skills and pocketbook. Compare the similar reasoning in *Trevor Ivory Ltd.v. Anderson*, [1992] 2 N.Z.L.R. 517 (C.A. Wellington).

<sup>52</sup> *Supra* note 10.

<sup>53</sup> *Supra* note 14.

<sup>54</sup> Cane raised similar concerns about a lack of definition: see *Tort Law*, *supra* note 12 at 350-51.

<sup>55</sup> The *Defective Premises Act 1972* (U.K.), 1972, c. 35, creates a warranty for successive owners of dwellings. Only commercial buyers are thus affected by *Murphy*, *supra* note 14.

<sup>56</sup> *The Aliakmon*, *supra* note 1 at 817 and 820.

And how can we reconcile this principle with the justification frequently voiced for recognizing a tort duty, that the relation between the parties was “akin to contract?” For, if that was indeed the case, why did the parties not “go the extra mile,” and form a contract? In *Hedley Byrne*, for example, the relationship between the defendant bank and the plaintiff, to whom the former had furnished a credit report through his own bank’s mediation, was described as “the equivalent of contract.”<sup>57</sup> In the controversial *Junior Books* case, which allowed an owner to sue a subcontractor in tort for applying defective floor polish which subsequently needed replacement, the relation between the parties was described as “only just short of direct contractual relationship.”<sup>58</sup> And though that decision has been widely disparaged in later cases, the argument was heard again in *Smith*, where the purchaser of the “modest home” was deemed to be in a relation “akin to contract”<sup>59</sup> with the valuer employed by the prospective mortgagee. Admittedly, the fact that the cost of the valuation was debited from her account confirmed the reality of the description. In none of these cases was it so much as hinted that the plaintiff could have taken the opportunity to protect herself by contract.

Cases such as *Edgeworth Construction* suggest the question of how to justify requiring the plaintiff to protect himself or herself by contract, when the defendant had an equal opportunity of contracting for exemption. (In *Edgeworth Construction* the Court did not require the plaintiff to do so). Stapleton faces this issue bravely:

It is true that where it is found that P could have secured the deterrence-generating protection described and a duty is denied, the negligent D escapes liability. But this will only appear to be startling if we maintain the lopsided view that duty is generated by defendant behaviour alone. If the interest the law takes elsewhere in P’s capacity for self-protection is addressed consistently by being considered also at the duty stage, we would not be so surprised to find that the price of under-deterrence involved in such escapes from liability is sometimes seen, and legitimately seen, as outweighed by pursuit of incentives against free-riding.<sup>60</sup>

Apart from anything else, this value preference leaves unanswered the crucial question of when, indeed, such incentives against free-riding might be justified. If anything, the running comment

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<sup>57</sup> *Supra* note 47 at 530.

<sup>58</sup> *Supra* note 21 at 533.

<sup>59</sup> *Supra* note 42 at 846.

<sup>60</sup> “Alternative Opportunities,” *supra* note 43 at 332.

throughout Stapleton's article conveys an impression of its general application.

At least two reasons give us pause. First, the suggested sanction against free-riding seems not only unduly harsh, but runs counter to the historical progress of tort law from long before the putative excesses of the 1960s and 1970s. The universal revulsion against the contributory negligence bar and its replacement by the more qualified formula of apportionment tells a pertinent story. The drastic sanction against "free-riding," an offence which strikes one as less heinous than the paradigmatic contributory negligence, looks like a disproportionate response to the imagined evil. Second, as McLachlin J. pointed out in her concluding remarks for the Court in *Edgeworth Construction*, "[o]ne important policy consideration"<sup>61</sup> weighs against those in the position of the defendant engineering firm: for, to require the contractor to conduct a thorough professional review of the engineering design would involve needless duplication of effort—a waste of economic resources for the minor aim of encouraging self-discipline and thrift.

#### IV. CONCLUSION

The history of tort in the matrix of contract stretches back to *Winterbottom v. Wright*<sup>62</sup> if not beyond. For a time, it was accepted that a defendant's contractual undertaking pre-empted a corresponding tort duty, not only to the contractual partner, but also to third parties. *Donoghue*<sup>63</sup> exploded this "privity fallacy" in relation to claims for personal injury and damage to property. The fact that the defendant owed a contractual obligation to A did not preclude the defendant also owing a tort duty in the same matter to B. But other constellations of the contract matrix raised new problems, mainly in the context of purely economic loss, once the door to such claims was pushed slightly ajar by *Hedley Byrne*. A common feature is their setting in a planned transaction.

One such problem concerns the effect of a contractual limitation clause on the tort liability of a third party. This can be resolved either by expanding the reach of contract beyond privity, or by "jumping the privity gap" in tort. The first part of this paper attempted to deal with

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<sup>61</sup> *Supra* note 50 at 220-21.

<sup>62</sup> (1842), 10 M.& W. 109, 152 E.R. 402 (Ex. Pl.).

<sup>63</sup> *Supra* note 7.

various attempts to follow the tort route. Whether this is preferable to the contract approach is quite another matter. It might be interesting to speculate on why British courts adopted the one approach, while American and Canadian courts inclined to the other. The answer, I believe, lies in the comparative flexibility of American and Canadian contract and tort rules. Whatever might be said in general about the adaptability of the modern law of contract to changing social demands,<sup>64</sup> the privity rule has, in British perspective, assumed a unique aura of untouchable classicism despite its relatively modern provenance. By contrast, tort law has become free-flowing despite occasional cyclical setbacks, such as those recently experienced. Resort to tort is therefore seen as the only feasible avenue to the desired outcome, in much the same way that German law, conversely, has been forced into contract routines in order to escape the straitjacket of its outdated Code regime of tort.<sup>65</sup> In contrast, American and Canadian courts have felt freer to choose between contract and tort without comparable doctrinal constraints. In the present context, their preference for the contract approach is undoubtedly due to the perception that it is the more appropriate and effective way of dealing with a matter that arises in a matrix of contract, and does not call for a last resort remedy of tort.

The other problem, in the context of a contract network, is what effect to attribute to a plaintiff's failure to seize an opportunity for preemptive protection by contracting with the injurer or a third party. This raises an issue of a different order, not the more or less technical one of which road to travel to a desired destination, but one of substantive policy. Should the protection of tort law be denied to a person capable of advance planning against the risk? The emphasis on individual responsibility in the political and economic ideology of the recent past has provided support for this argument, but its place in received doctrine must await further testing.

Both situations illustrate the weakening of the borders between contract and tort, that were once so clearly delineated by the classical theorists of both disciplines. Over twenty years ago, Grant Gilmore presaged the *Death of Contract*<sup>66</sup> noting the ongoing absorption of

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<sup>64</sup> A generally optimistic view was recently taken in D.W. McLauchlan, "The 'New' Law of Contract in New Zealand" [1992] N.Z. Recent L. Rev. 436.

<sup>65</sup> In the context of the problem discussed in Parts II and III, above, see H. Kötz, "The Doctrine of Privity of Contract in the Context of Contracts Protecting the Interest of Third Parties" (1990) 10 Tel Aviv Univ. Stud. L. 195.

<sup>66</sup> *Supra* note 8. See also P.S. Atiyah, *The Rise and Fall of Freedom of Contract* (Oxford: Clarendon, 1979).

contract into tort, among other factors, as the result of the socialization of contract law, once the stronghold of private ordering against intrusion by public policy. But that is only part of the story. In reality, the interaction between contract and tort has become reciprocal: if contract is being obliterated in some contexts, like concurrence, it has come to define the incidence of tort duties in others. This is especially apparent in the context of planned transactions which, until recently, fell within the exclusive domain of contract. As tort has expanded its reach into that sphere, it has learned to respect the important message of private ordering.

These developments surfaced at a time of growing judicial concern for ways to rein in the expansive, indeed explosive, potential of tort liability, especially of the law of negligence. Stapleton's distinguished writings<sup>67</sup> and my own paper are contributions to that debate.

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<sup>67</sup> See generally *supra* note 43.