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CASE UPDATES

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ARIZONA SUPREME COURT: DESIGN PROFESSIONAL NOT LIABLE IN TORT FOR PURELY ECONOMIC DAMAGE

6.14.22

By way of a recent Arizona Supreme Court holding, Arizona law continues to support the legal conclusion that non-contracting parties cannot maintain a cause of action sounding in negligence for purely economic damages. *Cal-Am Properties Inc. v. Edais Eng'g Inc.*, CV-21-0129-PR, 2022 WL 1613497, at *5 (Ariz. May 23, 2022).

PROFESSIONALS

Jodi L. Mullis

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THE PROBLEM

Cal-Am Properties, Inc. (Cal-Am) is a developer and operator of RV and mobile home parks. Cal-AM leased the Sundance RV Resort in Yuma, Arizona. Cal-Am leased it from the owner for the purpose of building a new banquet and concert hall on the property.

Cal-Am managed the project which was funded by the owner. Cal-AM hired VB Nickle as the contractor on the project who then hired Edais Engineering, Inc. (Edais). Edais was tasked with surveying the property and placing construction stakes to mark the permitted location of the hall. Edais later conceded that the placement of the stakes was defective and they were placed ten feet north of the plotted location. This required Cal-Am to adjust the site plan and subsequently eliminated eight RV parking spaces provided for in the original plan.

Cal-Am brought suit against Edais for various claims including negligence. The trial court found that only two contracts existed. One was formed between Cal-Am and VB Nickle and the other between VB Nickel and Edais. No contract existed between Cal-AM and Edais directly. Thus, the trial court granted summary judgment in favor of Edais and the trial court affirmed. *Cal-Am Props., Inc. v. Edais Eng'g Inc.*, NO.1 CA-CV 20-0279, 2021 WL 1422738 (Ariz. App., April 15, 2021). With the ruling, the Court concluded that Cal-Am could not maintain a claim against Edias.

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A BRIEF HISTORY OF THE CASE LAW

Since the two parties were not in contractual privity with each other, Cal-Am attempted to take an alternative avenue of potential recovery against Edias and filed a claim for negligence. Cal-Am claimed that Edais was negligent in the placement of the stakes and as a result, caused it economic harm.

In order to prove negligence a party must satisfy the following elements:

- A duty requiring the defendant to conform to a certain standard of care;
- A breach by the defendant of that standard;
- A casual connection between the defendant's conduct and the resulting injury; and
- Actual damages. *Gipson v. Kasey*, 214 Ariz. 141, 143 (2007)

The initial, general precedent for this type of construction claim was established by the holding in *Donnelly Construction Company v. Oberg/ Hunt/ Gilleland*, 139 Ariz. 184 (1984). The *Donnelly* court stated: "[d]esign professionals have a duty to use ordinary, skill, care and diligence in rendering their professional services" and confirmed that "such liability extends to foreseeable injuries and foreseeable victims which proximately result from...negligent performance of their professional services." In practice, this holding meant that the potential liability of design professionals extended beyond the business that they entered into a contract with, but also, extended to any other foreseeable plaintiffs. This precedent was good law until the *Gipson* case. *Gipson* overturned *Donnelly* and found that, "[f]oreseeability is not a factor to be considered by courts when making determinations of duty." The *Donnelly* decision is now rejected by Arizona courts.

So thought design professionals do owe certain duties, they only owe them to a more narrows class of parties. This is so because of the holding in *Gipson* which did away with the foreseeability factor. With this narrowed scope, the question remained whether Cal-Am could bring such a claim against Edias – two non-contracting parties.

THE IMPACT OF SPECIAL RELATIONSHIPS ON LIABILITY

The question then also turned on whether a special relationship existed between the parties in which case there would be a duty owed, and potential liability for a breach of that duty.

In the setting of negligence law, there are certain circumstances which give rise to a legal duty. Those can come in the form of special relationships between the parties. Special relationships require a pre-existing, recognized relationship between the parties. A special relationship includes, "common law relationships, those formed by contract, familial relationships, or joint undertakings." *Quiroz v. ALCOA Inc.*, 243 Ariz. 560 (2018). Examples of such relationships are:

- Landowner-Invitee
- Landowner-Licensee
- Employer-Employee
- Tavern Owner-Patron
- School-Student

Here, there is no evidence of a special relationship between Cal-Am and Edais. The two parties did not enter into a contract with one another and no other circumstances existed to show the existence of a special relationship triggering a legal duty. Although the parties engaged in a joint undertaking, this fact was not sufficient reason to make a finding that a special relationship existed between them.

In addition, Arizona does not include design professionals as a category of special relationships. The other jurisdictions that Cal-Am points to who have recognized design professionals as being in special relationships with owners and others, did not persuade the court in this case. The court expressly rejected and refused to adopt this approach and thus found that Edais did not have a special relationship with Cal-Am and therefore, did not owe them a legal duty. Another fatal blow.

PUBLIC POLICY AS A SOURCE OF LEGAL DUTY

In Arizona, the state statutes are the main source of duties based on public policy. For a statute to create a duty the following must be true:

- The plaintiff must be within the class of persons to be protected by the statute; and
- The harm must be of the type that the statute sought to protect against. *Quiroz* at 565.

Cal-Am contends that the statutes and regulations that establish minimum standards for design professionals establish a legal duty. The purported policy of these laws is to protect the safety, health and welfare of the public who utilize the services of design professionals. The court was not persuaded by this argument pointing out that this case does not involve the health or safety of any member of the public. Rather, it involves purely economic damage that Cal-Am suffered as the result of Edais' mistake. "Courts have a general reluctance to recognize tort duties to exercise reasonable care for the purely economic well-being of others." *Lips v. Scottsdale Health Corp.*, 224 Ariz. 266, 268 (2010).

The court found that the statutes and regulations were not designed to protect a plaintiff like Cal-Am, who had suffered only an economic injury. Cal-Am's argument that a design professional's duty of care is equivalent to that of a lawyer or doctor was faulty in the eyes of this court. They pointed out that these professionals owe a duty only to their clients, not to a potentially limitless amount of plaintiffs as is the case with design professionals. Therefore, the public policy established by Arizona's statutory and regulatory schemes do not support a finding of a legal duty on behalf of a design professional. This argument likewise failed.

COMMON LAW SOURCE OF DUTY

Cal-Am also argues that the Restatement (Second) of Torts establishes a duty on the part of Edais in this situation. Section 324A states, "[o]ne who undertakes, gratuitously or for consideration to render services to another which he should recognize as necessary for the protection of a third person, or his things, is subject to liability to the third person for physical harm resulting from his failure to exercise reasonable care to protect his undertaking." Restatement (Second) of Torts §324A (Am.L. Inst. 1965).

The court disagrees with Cal-Am's argument on this issue stating that it does not apply because Edais' faulty staking of the property did not physically harm the land itself. The mistake only affected the value of Cal-Am's economic interest in the property. Edais was hired by VB Nickle to place construction stakes according to the plans provides them by VB Nickle. This contract did not take into account any protection or potential impact of Cal-Am.

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Cal-Am then looks to the Restatement (Third) of Torts: Liability for Economic Harm §6 (Am.L.Inst. 2020), which imposes liability when one performs a service for the benefit of another if the entity providing the service fails to use reasonable care. The loss must be suffered by "the entity whose benefit the actor performed the service and through reliance upon it in a transaction that the actor intends to influence."

The reason this Restatement argument fails to apply here is because Cal-Am did not rely on Edais' staking of the property, but rather VB Nickle did. Edais would be liable to VB Nickle alone. The remedies available to Cal-Am clearly sound in contract rather than tort. The court also noted that design professionals are not insulated from liability, but their legal consequences should be litigated in this type of situation as a contract claim instead of a tort claim.

The end result of these efforts was to show that Cal-Am's proper remedy was to bring suit against VB Nickle for breach of contract and Edias as a third-party beneficiary to the contract. Under the facts of this case, Cal-Am could not maintain a cause of action for negligence against Edias. So, though this holding narrows the scope of recovery that Cal-Am has for its' losses, it certainly does not bar Cal-Am from any recovery.