Simple Negligence and Economic Losses Don't Mix in Georgia

Every business litigator frequently confronts claims of economic losses, particularly lost profits. And every such claim is typically met with a standard arsenal of defenses: the profits alleged to have been lost are too speculative to be recovered, or the losses were caused by something other than the defendant's conduct. But there is one defense that, by its nature, can spell complete damnation for an economic loss recovery when it is premised on a claim of negligence—Georgia's economic loss rule. Although some form of the rule prevails in every state, Georgia courts have bestowed unusual austerity and breadth upon the doctrine, doing so in somewhat unpredictable fashion. This article briefly traces the evolution of the economic loss rule in Georgia, sets out the current state of the law, and concludes by addressing whether Georgia courts should reverse course and restrict the doctrine's application.

The Tort Versus Contract Dilemma

Georgia courts have long grappled with the intersection and overlap of contract and tort claims. The question was often this: when can a party to a contract recover economic damages from the other contracting party for mere negligence in carrying out her contractual duties? Seemingly conflicting answers emanated from the reported decisions. *Compare Long v. Jim Letts Oldsmobile, Inc.*, 135 Ga. App. 293, 294, 217 S.E.2d 602, 604 (1975) ("It is well settled that misfeasance in the performance of a contractual duty may give rise to a tort action.") with *Mauldin v. Sheffer,* 113 Ga. App. 874, 879-80, 150 S.E.2d 150, 154 (1966) ("[T]he rule may be fairly deduced that in order to maintain an action [in tort] because of a breach of duty growing out of a contractual relation the breach must be shown to have been a breach of a duty imposed by law and not merely the breach of a duty imposed by the contract itself.").

Although Georgia courts struggled to articulate the precise formulation of the rule, the actual results of their decisions were generally consistent. The appellate courts essentially precluded parties to a contract from recovering in negligence for economic losses resulting from negligent performance of contractual duties, but allowed such claims where they were premised on a professional or "special" relationship between the parties. *Compare Orkin Exterminating Co. v. Stevens*, 130 Ga. App. 363, 366, 203 S.E.2d 587, 591 (1973) (disallowing claim for economic losses based on negligent performance of contractual duty to properly treat termite infestation) with *Mauldin v. Sheffer*, 113 Ga. App. 874, 150 S.E.2d 150 (1966) (allowing negligence claim for economic losses against professional mechanical engineer).[1] These special contractual relationships include, for example, those between principal and agent, bailor and bailee, attorney and client, physician and patient, carrier and passenger or shipper, and master and servant. *Bulmer v. Southern Bell Tel. & Tel. Co.*, 170 Ga. App. 659, 660, 317 S.E.2d 893, 895 (1984). Such negligence claims are allowed, despite arising from a contractual duty, because the law imposes a duty of care for these special relationships that is independent of the duty imposed by the contract itself. *Id.*

The Economic Loss Rule in Products Liability Cases

[1] *See also* O.C.G.A. § 51-1-11(a) ("Except as otherwise provided in this Code section, no privity is necessary to support a tort action; but, if the tort results from the violation of a duty which is itself the consequence of a contract, the right of action is confined to the parties and those in privity to that contract, except in cases where the party would have a right of action for the injury done independently of the contract….").

When the appellate courts were shaping modern-day products liability law in the 1960s and 1970s, a narrower question regarding economic losses arose: are they recoverable in negligence when a defective product fails? The Georgia appellate courts decided that plaintiffs can recover in tort for personal injuries and damage to other property, but recovery for loss of value or use of the thing sold, or the cost of repairing it, is not permitted. *Long v. Jim Letts Oldsmobile, Inc.*, 135 Ga. App. 293, 217 S.E.2d 602 (1975); *Flintkote Co. v. Dravo Corp.*, 678 F.2d 942, 948 (11th Cir. 1982); *Vulcan Materials Co. v. Driltech*, 251 Ga. 383, 387-88, 306 S.E.2d 253 (1983); *Advance Drainage Sys. v. Lowman*, 210 Ga. App. 731, 733, 437 S.E.2d 604, 607 (1993). Thus, if a plaintiff purchases a defective car that stops running, the buyer cannot maintain a negligence claim against the seller for diminution in value, repair costs, and loss of use. *Jim Letts*, 135 Ga. App. at 295. In such a case, the plaintiff must resort to a contract warranty action to obtain compensation.[2]

The rationale for this limitation is straightforward: "when a defective product has resulted in the loss of the value or use of the product itself, or the cost of repairing it, the plaintiff is merely suing for the benefit of his bargain." *Jim Letts*, 135 Ga. App. at 295. The contract under which the plaintiff purchased the product is intended to address such damages. This reasoning makes sense in the context of product liability cases, for where two parties have entered into a sales contract for a product, contract warranty law should dictate the scope of the buyer's remedies for the product's failure to meet the buyer's bargained-for expectations.

Extension of the Rule

But what started out as a sensible restriction in products liability cases has morphed into a broad shield in other areas, as Georgia courts have extended the economic loss rule well beyond its original roots. *See City of Atlanta v. Benator*, 310 Ga. App. 597, 605, 714 S.E.2d 109, 116 (2011) ("More recently, however, both the Georgia Supreme Court and this court have applied the economic loss rule outside of product liability cases."). The Georgia Supreme Court first approved of such a broader application in *General Electric Co. v. Lowe's Home Centers*, 279 Ga. 77, 608 S.E.2d 636 (2005). There, the plaintiff, Lowe's, sought to replace its retail store in Rome with a much larger superstore, which would require the acquisition of adjacent property. Lowe's entered into a lease agreement with a developer who had a purchase option on the property, but the arrangement was canceled when Lowe's learned that a nearby General Electric plant had environmentally contaminated the property. Lowe's brought a negligence claim against General Electric and won a jury verdict for lost profits in the amount of $18 million.

On appeal, the Georgia Supreme Court ruled that Lowe's' lost profits were not recoverable in negligence because of the economic loss rule. 279 Ga. at 79. This conclusion was remarkable because the court applied the rule to a case that did not involve products liability, clearly approving use of the

[2] The courts later adopted an "accident exception" to the rule. The accident exception provides that the economic loss rule does not preclude recovery for damage to the defective product itself where the product is damaged by a "sudden and calamitous" event which "poses an unreasonable risk of injury to other persons or property." *Vulcan Materials Co. v. Driltech, Inc.*, 251 Ga. 383, 386-87, 306 S.E.2d 253, 256-57 (1983). So if the defect in the above-cited *Jim Letts* case had caused the car to catch fire, the buyer could have recovered in negligence for property damage to the car itself (and any personal burn injuries the buyer may have suffered). *See id.* In addition, Georgia courts have excepted claims of negligent misrepresentation from the economic loss rule. *See City of Cairo v. Hightower Consulting Engineers, Inc.*, 278 Ga. App. 721, 729, 629 S.E.2d 518, 525 (2006); *Holloman v. D.R. Horton, Inc.*, 241 Ga. App. 141, 148, 524 S.E.2d 790, 796-97 (1999).

doctrine in other contexts. Indeed, the court articulated the rule in a much broader sense, stating that "[t]he economic loss rule generally provides that a contracting party who suffers purely economic losses must seek his remedy in contract not in tort." *Id.* at 78.

Taking the Supreme Court's lead, the Court of Appeals has applied the economic loss rule in other non-products cases. In *Remax The Mountain Co. v. Tabsum, Inc.,* 280 Ga. App. 425, 427-28, 634 S.E.2d 77, 78-79 (2006), the court held that several businesses could not recover lost profits caused by the defendants' negligent dumping of groundwater on nearby property, which washed away a road and rendered it difficult for patrons to access the plaintiffs' business locations. This holding marked another expansion of the rule because neither a product nor a contract was involved. The court expressly acknowledged its expanded application of the doctrine: "Although the economic loss rule is more often applied in the context of products liability cases or to distinguish between those actions cognizable in tort and those that may be brought only in contract [citation omitted], the reasoning behind the rule, as set forth in *Lowe's*, seems equally applicable to the situation here." 280 Ga. App. at 427 n.5.

A year later, in *J. Kinson Cook of Ga. v. Heery/Mitchell*, 284 Ga. App. 552, 644 S.E.2d 440 (2007), the Court of Appeals held that a general contractor could not maintain a negligence claim for increased construction costs against a construction manager hired by the property owner because the contractor and manager were not in privity of contract, and the contractor did not assert any legal duty that the manager owed independent of the contract between the owner and contractor. 284 Ga. App. at 555-56. Just as in *Tabsum,* a defective product was not at issue and the parties were not in contractual privity with one another. Indeed, the court's rationale is somewhat ironic; while other decisions have precluded negligence claims *because* of a contractual relationship, the court here cited the *lack* of contractual privity as a basis for dismissal. *Id.*

More recently, the Court of Appeals held that plaintiffs cannot seek utility overpayments made because of negligent billing by a contractor. *City of Atlanta v. Benator*, 310 Ga. App. 597, 605-06, 714 S.E.2d 109, 116 (2011). In *Benator*, the plaintiffs sued a city contractor alleging that they were negligently overcharged for water and sewer service. Upholding dismissal of their claims pursuant to the economic loss rule, the Court of Appeals reasoned that the plaintiffs were only seeking overpayments of money—not "damages due to injury to their persons or to their real or personal property." 310 Ga. App. at 606. Just like the *Tabsum* and *Heery/Mitchell* cases, this case involved neither a defective product nor parties in contractual privity.

Distilling the Applicable Rule

Given the economic loss rule's continued expansion, it has become difficult to articulate its precise definition outside the context of products liability. The Georgia Supreme Court made an effort to do so, explaining that "[t]he 'economic loss rule' generally provides that a contracting party who suffers purely economic losses must seek his remedy in contract and not in tort." *Lowes Home Centers*, 279 Ga. at 78, 608 S.E.2d at 637. However, we have already seen that this definition is insufficient, for the rule has been applied where the plaintiff and defendant were not in privity of contract, *see Benator*, *supra,* and even where there was no contract involved in the case at all, *see Tabsum, supra*.

In reality, the prevailing general rule in Georgia is much broader than the appellate courts seem willing to expressly admit. It appears that the current rule is this: absent personal injury or property damage, a plaintiff may not recover purely economic losses for negligence except in cases involving a special relationship (e.g., professional malpractice). There is no requirement that the plaintiff be a "contracting party," and there is certainly no requirement that a defective product to be involved.

Is it Time to Rein in the Rule?

Like Georgia courts, Florida's appellate courts have historically confronted an elusive and evolving economic loss rule susceptible of varying applications. *See Tiara Condo. Ass'n v. Marsh & McLennan Cos.*, 2013 WL 828003, at *2 (Fla. Mar. 7, 2013) ("The exact origin of the economic loss rule is subject to some debate and its application and parameters are somewhat ill-defined."). In *Tiara*, however, the Florida Supreme Court decided to finally put an end to the confusion, overturning decades of case law by eliminating the economic loss rule for all cases except those involving products liability. *Id.* at *8. The court acknowledged that it had "issued a number of rulings which … appeared to expand the application of the rule beyond its principled origins and have contributed to applications of the rule … well beyond [its] original intent." *Id.* at *6. Other appellate courts have adopted similar, albeit less drastic limitations. *See, e.g., Ins. Co. of N. Am. v. Cease Elec. Inc.*, 688 N.W.2d 462, 472 (Wis. 2004) (holding that Wisconsin's economic loss rule is inapplicable to claims for the negligent provision of services as opposed to products).

Perhaps it is time for Georgia to take Florida's lead and rein in the boundaries of the economic loss rule. Doing so would bring much-needed certainty and predictability to the doctrine, while at the same time allowing the courts to use other legal principles to address any real concerns of wide-ranging liability for economic losses. *See Lowe's*, 279 Ga. at 80 (discussing policy concerns about "expand[ing] the reach of Georgia tort law"). For example, in almost every non-products case discussed in this article, the court could have looked to threshold principles of legal duty and/or proximate cause to limit the recovery.[3] In *Lowe's*, the court's reliance on the economic loss rule was unnecessary because the court found that "Lowe's did not have a sufficient property interest in the adjacent land to permit recovery." *Id.* at 79-80. Because Lowe's premised its claim on damage to property that it only intended to lease in the future, Lowe's lacked a sufficiently concrete interest to recover for damage to that property. Thus, the Supreme Court could have simply held that Lowe's lacked standing or failed to establish proximate causation, instead of broadening the impact of the economic loss rule.

The same can be said for the *Tabsum* decision, where the plaintiffs claimed that a distant, non-adjacent landowner negligently washed away the road and hindered access to their businesses. 280 Ga. App. at 425. The court could have held that the alleged negligence was too far removed from the harm to satisfy the requirement of proximate causation. Similarly, the *Heery/Mitchell* decision could have been premised on the lack of a legal duty. Indeed, the court there specifically found that the plaintiff had "not asserted any legal duty that Heery owed independent of the contract." 284 Ga. App. at 556. Because a legal duty is an essential element of any negligence claim, the finding of no duty could have ended the court's analysis without reference to the economic loss rule.

[3] *See*, *e.g.*, *White v. Rolley*, 225 Ga. App. 467, 469, 484 S.E.2d 83, 86 (1997) ("The concept of proximate cause acts as a limitation on what would otherwise be the unlimited liability of a negligent tortfeasor for all the immediate and eventual consequences of his negligence.").

However, Georgia need not go so far as Florida and restrict the economic loss rule to products liability cases only. In addition to products cases, the rule should remain applicable to prevent a contracting party from recovering economic losses from the other contracting party in negligence when the claim is premised on breach of a duty existing solely by virtue of the contractual relationship.[4] Just as in products liability cases, allocation of risks and benefits regarding economic losses can be negotiated between the parties and dictated by agreement; allowing a negligence claim would simply allow an aggrieved party to effectuate an after-the-fact circumvention of the parties' bargained-for exchange. Defining and applying the economic loss rule in this manner would pay respect to the doctrine's original intent while restoring analytical certainty to its application.

About the Author:

Stacey A. Carroll
Attorney-at-Law
CARROLL LAW FIRM LLC
1380 West Paces Ferry Rd., NW
Suite 2100
Atlanta, Georgia 30327
Phone: 404.816.4555
Fax: 404.481.2074
Mobile: 770.714.8023
www.carroll-firm.com

Stacey Carroll is an experienced trial lawyer who represents those who have been harmed by the negligence, intentional misconduct, or wrongful business practices of others. Stacey spent the first several years of his career representing large corporations in high stakes litigation. He now uses that invaluable experience to aggressively represent individuals and smaller businesses. Stacey has litigated hundreds of civil lawsuits for both individuals and businesses, many of which involved millions of dollars in damages. He has first-chaired jury trials in Georgia, South Carolina, and Tennessee, and has been recognized as a "Rising Star" in the legal profession by Georgia Super Lawyers magazine.

[4] As applied in the general contract versus tort scenario, the courts might be well served to simply call the doctrine something else, such as "contractual preemption." The doctrine would simply provide that, where the parties have clearly bargained for risks and benefits in a contract, a general tort duty of care cannot be asserted to circumvent that agreed bargain with respect to the subject matter of the agreement.