

MINIMIZING ENGINEERING LIABILITY EXPOSURE

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Minimizing Engineering Liability Exposure

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UNDERSTANDING AND MINIMIZING LIABILITY UNDER CONTRACT

By Jeffrey A. Schoen

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Section 1

UNDERSTANDING (AND MINIMIZING) PROFESSIONAL NEGLIGENCE ACTIONS

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UNDERSTANDING AND MINIMIZING PROFESSIONAL NEGLIGENCE ACTIONS

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I. OVERVIEW

Engineers, like many other design professionals, are subject to third party claims for negligence, in instances where foreseeable harm results from their substandard work.

This type of claim is called a “tort” claim because it is a “wrong” that does not depend on the existence of a contractual obligation but, rather, arises out of the “duty” imposed on the party as a matter of law. The relationship of the parties determines the nature and existence of this “duty” imposed. Therefore, a third party that is not a party to the engineering contract, may still claim that the foreseeability of the harm to it was to be anticipated by a faulty engineering plan or design and sue in negligence against the engineer even if they never met or knew one another and had no relationship, contractual or otherwise.

We must distinguish here from what we call a first party claim- i.e. a claim brought in contract, by a contracting party for breach of the terms of that contract, or for implied covenants arising under contract, such as the covenant of good faith and fair dealing implied in every contract. This covenant presupposes an obligation on a contracting party as a matter of law to not prevent or interfere with the other party’s ability to enjoy the benefit of its bargain. While this is referred to sometimes mistakenly as a “duty” it is not to be confused with a tort type duty leading to a negligence claim. The breach of the implied covenant of good faith is a contract based claim. A claim arising out of a contract (i.e. that cannot exist “but for” the contract) is subject to a discretionary award of reasonable attorneys’ fees under A.R.S. § 12-341.01 (A) or a mandatory award of reasonable attorneys’ fees under the express terms of a contract.

There are no attorneys’ fees awardable in a purely tort type claim like negligence.

Therefore, the breach of a contract rests on an express or implied breach of the written or oral contract between the parties and the damages that are contemplated by the parties at the time of contracting that arise naturally and directly from the breach. Whereas, the tort of negligence does not rest on any breach, or duty arising out of the contract terms or language, but rather is based on duties created by law. These duties generally arise out of public policy and require a party to act “reasonably” under the “circumstances” so as to avoid damage to others that is foreseeable.

Tort damages are also distinguishable from contract damages in that consequential or other damages that naturally flow from the tortious conduct, regardless of whether contemplated, may be collected.

Finally, there are parties to a contract may want to sue not only under the contract, but also in tort for negligence as well. For purpose of our discussion, you should be aware of the "economic loss rule," adopted in Arizona. In summary, this rule of law (described more below) generally establishes that where there are purely economic losses in nature that result from the breach of a contract, tort remedies and claims should be subsumed into the contract remedy, and therefore it is not appropriate to sue in negligence. We will discuss application of this general rule and how it may apply to claims against engineers.

II. ELEMENTS OF A PROFESSIONAL NEGLIGENCE CLAIM AND UNDERSTANDING THE DUTY OF CARE AND STANDARD OF CARE

Negligence is often defined as consisting of a breach of duty. That is wrong in the sense that the duty in such a case can be defined only as a duty to use due care, i. e., not to act negligently; and to define the duty so, and then to define negligence as consisting of a breach of the duty, is to define in a circle. The misconception has arisen from a failure to distinguish between a negligent wrong, which, like all wrongs, involves a breach of duty, and the negligence itself, which is one element in the wrong. It is true that negligence which in the particular case is not a breach of any legal duty is of no legal importance; but that does not touch the question of its nature as negligence.

There are many cases where the law does not require care, where therefore the act of negligence is not legally wrong; but it is none the less negligence. We must have a conception of negligence as it is in itself, independent of the conception of duty, in order that we may use it as a condition in the definition of various duties.

In negligence cases, architects and engineers were historically insulated from liability upon complete performance based on the courts' recognition of two effective defenses: lack of privity between the design professional and the injured party and acceptance of the work by the owner. [FN1] In previous years, the judgment of architects and engineers concerning the preferred design, the kind of specifications utilized or the supervision of construction was seldom challenged. In fact, liability regarding designs was restricted to construction parties. [FN2]

In recent times, actions against architects and engineers have grown by at least twenty percent. Furthermore, since 1960, the cost of architect and engineer malpractice disputes has increased threefold. [FN3] One writer has identified several reasons why the number of professional negligence suits against architects and engineers has multiplied:

First, new materials are frequently used that are not fully tested Second, the increasing complexity of construction projects has made it more difficult to determine who is really at fault [Third], [t]here has been a definite change in attitudes towards litigation [Fourth], the belief that the government should provide protection against

everything undesirable, as indicated by the increase in government regulations and class action litigation [Fifth], designers are trained to solve problems, not litigate. Their methods are open, methodical, and provide many points of vulnerability. Finally, the design profession involves many decisions based on judgment. [FN4]

Currently, the traditional cloak of protection surrounding the design professional in negligence suits no longer prevents the injured plaintiff from recovering. This change in treatment is due to the arrival of liability insurance and the increased interest in providing the injured person with sufficient compensation to restore him to status quo. [FN5]

A number of theories may be asserted against engineers for misconduct related to their professional duties. Some of the civil causes of action will be identified briefly. More specifically, we will briefly touch on here today only the following: professional, intermediate, and strict liability standards; res ipsa loquitur; expert testimony; causation; damages; liability of engineers based on negligent designs, supervisory responsibilities, inspections, preparation of plans and specifications, issuance of certificates, and various defenses. We will also touch on damages issues and who can bring a claim.

A. DEFINITIONS OF DIFFERENT STANDARDS

Engineers are design professionals. The engineer is “one who is trained . . . in a branch of engineering” that has been described as “[t]he application of scientific and mathematical principles to practical ends such as the design, manufacture, and operation of efficient and economical structures, machines, processes, and systems.” [FN7] Both the architect and the engineer are involved in planning, designing, supervising, and maintaining safety standards in connection with the construction of buildings or other large structures. Consequently, both professionals receive parallel treatment under the law for the purpose of assessing issues involving their duty of reasonable care and liability for negligent conduct. [FN8]

1. SCOPE OF DUTY; BREACH; CAUSATION; DAMAGES

As indicated by the court in a case against an architect, negligence actions in general require that the plaintiff prove the existence of a duty owed by the defendant, the breach of that duty, and that the defendant's breach proximately (factually and legally) caused an injury to the plaintiff, resulting in actual damages. [FN9]

a. Duty; Breach of Duty

Three factors comprise the duty element: affirmative duty, foreseeability, and standard of care. In order for a breach to occur, there must be a departure or deviation by the defendant from the applicable standard. [FN10] Therefore, in the case of professionals who provide engineering services, the court considers whether reasonable care was used in performing those services. [FN11]

b. Professional Negligence Standard

Generally, individuals “performing engineering services are performing professional services, and the law imposes upon such persons the duty to exercise a reasonable degree of skill and care, as determined by the degree of skill and care ordinarily employed by their respective professions under similar conditions and like surrounding circumstances.” [FN12] This standard pertains to skills relative to problems encountered in architecture, engineering and construction, which exceed the knowledge of the normal layperson. Note that this standard refers to the minimum level of performance, not the average or highest level of performance. [FN13] Thus, when an engineer, for example, fails to exercise reasonable care under the same or similar circumstances as “an engineer of ordinary prudence” would have exercised or when he does something contrary to this standard, the tortfeasor engineer may be held liable for professional negligence. [FN14]

c. Intermediate Standard

This midlevel standard is an alternative to the professional negligence standard. The intermediate standard is a high standard of care because it requires professionals to stay abreast of professional advances. In brief, this standard imposes a duty on the architect and engineer to stay informed. [FN15]

d. Strict Liability Standard

Another alternative to the professional negligence standard is the strict liability standard. Under a strict liability standard, a plaintiff could possibly recover from a structural engineer premised on two theories: “(1) a products liability claim based on a defective condition in the structure; or (2) a warranty claim based on representations made by the engineer.” [FN16] For instance, if the product complained of is a completed building, the structural engineer may be held strictly liable to the owner for the harm produced by mistakes in design or construction. Since strict liability is not based on fault, it is irrelevant that the engineer “exercised all possible care” in designing the structure. [FN17]

Although there is opposition to the imposition of strict liability on engineers and architects, a limited number of plaintiffs have prevailed. Nevertheless, there is a trend towards the application of strict liability to construction professionals when a plaintiff sustains harm on the premises.[FN18] New York appears to have embraced this position with the condition that the defect that produced the harm was a latent one. Although there is resistance, many jurisdictions are unequivocally moving towards the imposition of strict liability in suits involving builders, contractors, and vendors of real estate. [FN19]

In sum, any of the preceding standards, if applicable, ordinarily constitute a breach of duty by the engineer professional. However, as stated by one court, due to the absence of the elements needed to prove the applicability of strict tort liability, professional services normally do not lend themselves to liability without fault. [FN20]

e. Causation; Damages

Factual cause and legal cause connect the breach of duty and damage elements which subject the engineer to liability for professional negligence. To satisfy both duty and legal cause, both the plaintiff and the risk or consequences must be reasonably foreseeable to the defendant. Courts have stated that design professionals may be held liable for the foreseeable consequences or injuries to foreseeable victims, which proximately result from unreasonable care in the preparation of structure designs or in the performance of professional services in general. [FN21] In other cases, proximate cause was lacking in actions against architects and engineers based on negligent design or supervision of construction. [FN22] A plaintiff who sues based on architect or engineer malpractice may seek damages for economic loss, physical harm, mental anguish, medical expenses, lost wages, and so forth. If appropriate, punitive damages may also be requested. The economic loss rule prevents recovery unless certain types of harm have occurred as described hereinbelow in greater detail. Therefore, according to the majority rule, unless physical property damage or bodily injury has occurred, economic damages are not recoverable in negligence claims.

A relevant exception would allow recovery of economic loss to plaintiffs who are supervised by the engineer. Of course, the plaintiff in this situation should be a "known intended beneficiary" at the time the engineer's contract is being negotiated. [FN23] In brief, the courts have stated that an architect, for instance, may be held liable to a contractor who sustains economic loss brought about by the negligent conduct of the architect in connection with the construction project. Furthermore, courts have often declined to accept the assertion that privity of contract between the contractor-complainant and the architect is a prerequisite to proof of liability. [FN26]

2. RES IPSA LOQUITUR

The application of the res ipsa loquitur doctrine to negligence actions against engineers has been largely unsuccessful. Res ipsa loquitur means "the thing speaks for itself" which creates:

[a]n inference or rebuttable presumption of the defendant's negligence (unreasonableness) [that] arises in the following circumstances: (a) the event producing the harm was of a kind that ordinarily does not occur in the absence of someone's negligence, (b) the event was caused by an agency or instrumentality within the defendant's exclusive control, and (c) the event was not due to any voluntary action or contribution on the part of the plaintiff. [FN28]

III. EXPERT TESTIMONY

Expert testimony may be described as "[o]pinion evidence of some person who possesses special skill or knowledge in some science, profession or business which is not

common to the average man and which is possessed by the expert by reason of his special study or experience.” [FN31] As a general rule, in cases involving architects and engineers, expert testimony is ordinarily necessary to establish the parameters of the professional standard and the breach of that standard. [FN32] Additionally, expert testimony is normally required in professional negligence cases to establish the standard of care even in the event of “clear and palpable” negligence. [FN34] It is the law in this jurisdiction for many years that expert testimony is generally required to establish the standard of care in a case of professional negligence. *Asphalt Engineers Inc. v. Galusha*, 106 Ariz. 134, 135, 770 P.2d 1180, 1181 (1989). The exception to that rule is “...where the negligence is so grossly apparent that a lay person would have no difficulty recognizing it.” *Id.* at 1182.

Conversely, if the issues being litigated are comprehensible to the average juror, expert testimony is not essential to establish the standard of care and the breach thereof. [FN35] For example, expert testimony was not necessary in one case because the architectural error was so obvious that a layman was competent to judge the negligent act. [FN36] In another opinion, the court explained that expert testimony was not required in order for the plaintiff, a general contractor, to recover from the defendant, an architectural firm. The court made the following conclusion:

[T]estimony from an expert is not always necessary to establish the negligence of an architect acting in his professional capacity. When the matter in question is one that can typically be understood without assistance from an expert, when a layperson can infer negligence, then expert testimony is not required. [FN37]

In short, the necessity of expert testimony has been considered in a number of cases involving architects and engineers. Some courts have found it essential, and others have found it unnecessary. [FN38]

IV. LIABILITY TO THIRD PERSONS: PRIVACY CONSIDERATIONS

Originally, engineer defendants were not held liable to third persons who suffered harm while on improved real property mainly because such persons were not in privity of contract with the defendants. Also, duty to the parties to the contract ended upon completion and acceptance of the services. This older view also applied to builders, contractors, and vendors. [FN39]

Currently, privity of contract is not an essential element in every negligence action against engineers as required in the past.[FN40] A court in Rhode Island considered the question of “whether a third-party general contractor, who may foreseeably be injured or suffer an economic loss proximately caused by the negligent performance of a contractual duty by an architect/site engineer, has a cause of action in negligence against the architect/site engineer notwithstanding an absence of privity.” [FN41] Proof of duty, breach of duty, causation, and damages are required as proof of

negligence; however, privity of contract is not required in Rhode Island in order to maintain an action in tort.

Despite a lack of privity, a court in another case stated that the engineering firm that designed a steel warehouse could be held liable to injured construction workers. [FN42] For the most part, the law has moved away from the traditional privity of contract requirement in cases involving architect and engineer negligence. Consequently, where a swimming facility was designed by an architectural firm for a school, a student who was fatally injured while legally on the premises was owed a duty of care by the architects even in the absence of privity. Privity of contract was not a precondition to the imposition of liability. [FN43]

V. LIABILITY RELATED TO THE PREPARATION OF IMPROPER OR DEFECTIVE PLANS, DESIGNS, OR SPECIFICATIONS

Engineer professionals have a duty to exercise reasonable care in applying their skills, ability, and judgment to prepare plans, designs, and specifications that are correct and unflawed. Third persons (not parties to the contract) and others who actually contract for the services of these professionals may recover for the personal harm or death caused by the misconduct of these professionals. For example, various courts discuss an architect's or an engineer's duty of reasonable care in the preparation of improper or defective plans, designs or specifications in cases involving a negligently designed bus depot staircase; [FN44] improper preparation of plans for the remodeling of a school; [FN45] a negligently designed improvement to a municipal water pollution control plant by an architectural and engineering firm; [FN46] a negligently designed vestibule area containing a window into which plaintiff ran and received injuries; [FN47] and other relevant situations. [FN48] Note that generally, privity of contract is not a precondition to the imposition of liability on architects and engineers for negligent preparation of plans, designs or specifications.[FN49]

Since a plaintiff's injury may be caused by a patent or latent defect produced by improper plans, designs or specifications, many courts have restricted architects' or engineers' liability to injuries or death caused by latent or hidden defects, and other courts have imposed liability even if the defect was a patent or obvious one. [FN50]

VI. LIABILITY RELATED TO PERFORMANCE OR NONPERFORMANCE OF SUPERVISORY RESPONSIBILITIES

Injuries often occur during the course of construction work due to an engineer's negligent performance or failure to perform supervisory responsibilities. These professionals have a duty to exercise reasonable care in managing the workers and the job site, in complying with safety standards, and in taking other necessary precautions based on actual or reasonable awareness of risks during the course of construction work. In accordance with this duty, there is a generally accepted view that a supervising architect or engineer has an obligation to utilize the ordinary skills of his profession to protect any reasonably foreseeable person who may be injured while legally on the construction site.

[FN51] In addition to the professional reasonable person standard, supervisory responsibilities may also be imposed on architects and engineers by contractual provisions[FN52] and governmental regulations. [FN53]

VII. LIABILITY BASED ON IMPROPER ISSUANCE OF CERTIFICATE

Another function of the engineer is the issuance of certificates which is a written assurance or official acknowledgement or representation that certain work has been done. Ordinarily, construction contracts provide for a supervising architect or engineer to oversee construction and resolve issues over which there is dissension. In addition, the contractor may only be compensated for his work upon certification by the architect or engineer that the work was completed in a satisfactory manner. [FN54]

The general rule is that an engineer may be liable to one who sustains loss caused by negligent or incorrect issuance of a certificate concerning completion and quality of the work. However, if the professional has performed fully the duties imposed by the employment contract provisos, he will probably not be held liable for negligence. Many courts have stated that engineers are legally obligated to utilize reasonable care and skills of his profession in issuing certificates. If they fail to conform to this duty, they could be held liable to a building owner or possibly others for losses caused by incomplete or defective work which they certified. [FN55] Fraud or collusion in connection with the issuance of certificates by engineers causing damages is also prohibited and may result in liability. [FN56]

VIII. LIABILITY RELATED TO CONSTRUCTION OR MAINTENANCE OF HIGHWAYS OR BRIDGES

Engineers have been sued for negligence in connection with highways and bridge construction or maintenance. It is the generally accepted view that a civil engineer owes the public a duty to conduct himself competently and exercise reasonable care in designing control systems and in inspecting roads. If this duty is breached, and someone sustains damages therefrom, the engineer may be held liable to the claimant. [FN57] Liability may also be imposed on a county engineer if he is exercising a ministerial function as opposed to a discretionary one if injuries result.[FN58] Conversely, if an engineer is employed by the state, liability will probably not be imposed if his supervisory responsibilities do not include designing, participating in construction, or maintaining the road on which the victim was injured. [FN59]

IX. ADDITIONAL CLAIMS INVOLVING ENGINEERS

Litigation involving engineer misconduct is diversified and continues to multiply. Hence, the courts in recent years have been confronted with the following issues: negligent design by an architect; [FN60] an engineer's failure to ensure adequate venting and not providing a greater margin of safety; [FN61] an engineer's negligent issuance of a certificate of substantial completion; [FN62] an architectural firm's failure to install

detention screens in the hospital it designed; [FN63] reasonable foreseeability in a negligent-design claim; [FN64] a negligently designed viaduct; [FN65] statute-of-limitations defense by an architect; [FN66] expert testimony by an engineer regarding the competence of a builder's performance; [FN67] an architect's negligent design and construction of a pool; [FN68] immunity of an engineer who testified as an expert witness; [FN69] economic loss as a result of engineering and architectural negligence; [FN70] an engineer's failure to reject defective bridge components; [FN71] an engineer's failure to supervise a contractor's work; [FN72] and other miscellaneous issues related to architectural and engineering wrongdoing. [FN73]

A party is grossly or wantonly negligent if he acts or fails to act when he knows or has reason to know facts which would lead a reasonable person to realize that his conduct not only creates an unreasonable risk of bodily harm to others but also involves a high probability that substantial harm will result. *Walls v. Arizona Dept. of Public Safety*, 170 Ariz. 591, 595, 826 P.2d 1217, 1221 (1991).

It should be noted here that Arizona Revised Statutes ("A.R.S.") section 12-552 (2003) provides, in pertinent part: "[N]o action ... based in contract may be instituted or maintained against a person who ... performs or furnishes the design ... or construction ... of an improvement to real property more than eight years after substantial completion of the improvement to real property." A.R.S. § 12-552(A). (emphasis added)

X. DEFENSES

A. Contributory Negligence

Not only is a defendant required to use reasonable care to avoid harming others, but the plaintiff also has a duty to exercise reasonable care for his personal safety if he wants to recover damages from a negligent defendant. In one case against an architect of a construction project, the court found that the injured workman was contributorily negligent. [FN74] For this reason and others, the plaintiff was denied recovery. [FN75] In another case, the court did not feel that it was necessary that the plaintiff's requested instruction that the jury not consider her negligence in an action against an architect be submitted to the jury. Thus, the state supreme court concluded that the trial court's judgment favoring the architect was correct. [FN76]

B. Lack of Duty Owed

Duty, along with breach of duty, cause in fact, proximate or legal cause, and damage, must be alleged and established in order for an engineer to be subjected to liability for professional negligence. Therefore, if the plaintiff is unable to prove that the defendant owed a duty of care, negligent conduct cannot be proven. For example, one court declined to hold an architect, an engineer and a builder liable to subsequent purchasers of an apartment complex because the plaintiffs failed to show a duty owed. [FN77] Since the plaintiffs were not foreseeable persons, and there was no privity

between the plaintiffs and the defendants, the duty element could not be met; thus, no cause of action for negligence existed. [FN78]

C. Compliance With Approved Standards Of Practice

If an engineer's conduct conforms to recognized and approved standards of practice or safety, he may not be held liable for malpractice. Thus, where a plaintiff sued an architect who designed a building where the plaintiff's child suffered a fatal injury, the architect established that the prevailing standards were met in the construction of the balcony from which the child fell and died. [FN79] As stated by the court, "[a]rchitects are held to a standard of performance which requires them to employ that degree of skill and care ordinarily used by their colleagues." [FN80]

D. Patent Defects

An engineer may assert patent defect as a defense to a malpractice claim. Therefore, if the defect or condition that causes a plaintiff's injury is open and obvious or is not a latent or concealed danger, an engineer may be absolved from liability. [FN81]

E. Immunity

If a supervising engineer plays the role of a quasi-arbitrator between the parties, the immunity defense may be raised. Although these professionals may avoid liability under this defense, a number of cases have disregarded their quasi-arbitrator function and held supervising architects and engineers, who have negligently issued certificates of progress or completion of the work, liable to the injured plaintiffs. [FN82]

F. Statute Of Limitations

If the statute of limitations has run, no suit shall be maintained against a negligent engineer. One court has stated that "a negligence cause of action accrues as soon as the plaintiff is entitled to maintain the action, i.e., at the time of the first legal injury, regardless of whether the full amount of the damages is apparent." [FN83] In another case for negligent design of a ventilation system, the court stated "[i]n suits alleging architectural malpractice, the action accrues either when the design is submitted to and accepted by the owner or upon substantial completion of the building." [FN84] In a third suit against a soil engineer for negligence related to an investigation and analysis of a new building that was being constructed, the general rule was that the statute of limitations begins to run, with respect to a construction contract, upon completion of the work. [FN85] It was also stated by the court that the limitations statute is subject to the discovery rule in particular instances. This rule states "the limitations period does not begin to run until the date the plaintiff knew or should have known of the injury." [FN86] It should also be noted that some state laws allow the discovery rule to toll the limitations period. Fraud or concealment by a defendant could also have a tolling effect. [FN87]

In sum, the statute of limitations may begin to run against an architect or engineer at the time of the negligence, at the time that the plaintiff discovers or should have discovered the damage or injury, or at some other time. [FN88]

G. Economic Loss Rule As It Pertains To Professional Negligence

In *Flagstaff Affordable Housing Ltd. Partnership v. Design Alliance, Inc.*, 223 P.3d 664 (2010), the Arizona Supreme Court held that, because of the economic loss rule, “a contracting party is limited to its contractual remedies for purely economic loss from construction defects.”

As a threshold matter, the Court defined “economic loss” as “pecuniary or commercial damage, including any decreased value or repair costs for a product or property that is itself the subject of a contract between the Plaintiff and defendant, and consequential damages such as lost profits.”

A claim for punitive damages does not alter any of the analysis found in *Flagstaff Affordable Housing* and the economic loss rule. Punitive damages are “extracompensatory” and “go beyond any obvious elements of compensation” that traditional damage awards are meant to provide. Dan B. Dobbs, *The Law of Remedies* at 310 (2nd ed. 1993).

The facts of that case are that *Flagstaff Affordable Housing Limited Partnership* (Owner) contracted with *Design Alliance, Inc.* (Architect) for the design of eight apartment buildings and a community center. One requirement of the design was that it comply with the federal Fair Housing Act's accessibility guidelines. Several years after the buildings were constructed, the U.S. Department of Housing and Urban Development filed a complaint against Owner, alleging that the buildings violated the accessibility guidelines. After Owner settled that claim, Owner sued Architect for both breach of contract and negligence.

Owner voluntarily dismissed its breach of contract claim and its negligence claim was the only claim at issue. Owner conceded that it sought to recover only economic losses.

The superior court dismissed the complaint, but the Court of Appeals reversed the dismissal and held that the economic loss rule does not bar negligence claims against design professionals. On review to the Arizona Supreme Court, the Court vacated the Court of Appeals opinion and remanded the case back to superior court for further proceedings.

In reaching its holding that a contracting party is limited to its contractual remedies for purely economic loss from construction defects against design professionals the Arizona Supreme Court focused on the “underlying policies of tort and contract law in the construction setting.” In particular, the Court stressed the contract law policy of “upholding expectations” and encouraging parties “to order their prospective

relationships, including the allocation of risk of future losses and the identification of remedies, and to enforce any resulting agreement consistent with the parties' expectations.”

In light of that policy, the Court found that imposition of “common law tort liability in addition to contractual remedies” was improper when common law contract remedies already provide for the recovery of costs of remedying the defects and other damages reasonably foreseeable to the parties upon entering the contract.

The Court ultimately concluded that the analysis previously applied by the Court of Appeals in determining whether to apply the economic loss rule was misguided as applied to construction defect cases. In addition, the Court found that the question of whether a contracting party has waived their tort remedies and will be limited to contractual remedies to be irrelevant to whether the economic loss doctrine applies. Rather, the Court made clear that “a party will be so limited unless the parties have provided in their contract for tort remedies.” *Id.* at ¶ 29.

Ironically, the Supreme Court attempted to limit *Flagstaff*'s holding, stating that the economic loss rule does not apply to attorneys or, necessarily, to other professionals, and that it should not be applied with a broad brush. 223 P.3d at 673. But, this has largely been interpreted so far as to mean that where there is a “fiduciary duty” owed to a contracting party, such as with lawyers and clients, the rule will not bar tort claims.

Thus, the holding in *Flagstaff* was simply that a plaintiff who contracts for construction cannot recover in tort for purely economic loss, unless the contract otherwise provides. The key move the Court made was to restore the concept of privity of contract to the central place it held in ELR jurisprudence prior to *Carstens*. *Carstens* was a case in which a city and its building inspector was sued for alleged grossly negligent inspection of construction. The Court of Appeals in *Carstens* disallowed the claim to proceed against the inspector based on the ELR even though no contract existed between the parties. The Supreme Court rejected the “overly broad” formulation of the ELR from *Carstens* on which some subsequent courts had relied, noting, “[I]n many contexts, tort recovery is available for solely pecuniary losses.” At the heart of the case, the Court said that describing the ELR in an overly broad way:

“conflates two distinct issues: (1) whether a contracting party should be limited to its contract remedies for purely economic loss; and (2) whether a plaintiff may assert tort claims for economic damages against a defendant absent any contract between the parties. As explained below, we believe the economic loss doctrine is best directed to the first of these issues, and we use the phrase to refer to a common law rule limiting a contracting party to contractual remedies for the recovery of economic losses unaccompanied by physical injury to persons or other property.

Indeed, the Court said, “[T]he principal function of the economic loss doctrine, in our view, is to encourage private ordering of economic relationships and to uphold the expectations of the parties by limiting a plaintiff to contractual remedies for loss of the

benefit of the bargain. These concerns are not implicated when the plaintiff lacks privity and cannot pursue contractual remedies.”

The practical result and effect of all this to the engineer or other design professional in the end is rather simple. If a contract exists and reasonably and clearly limits the parties contractual remedies, then there will be no tort claim for negligence or otherwise for purely economic type losses that result from a breach. A professional services contract that limits the scope of its liability in regard to economic losses will generally be upheld. However, if there is personal injury or personal property damages present, then a negligence claim for those damages will be upheld beyond the purely contractual remedies recovered under the contract claim. And, in the recent case of *Cook v. Orkin Pest Control*, 227 Ariz. 331, 258 P.3d 609 (App. 2011) the Court held that even a fraudulent inducement claim would be barred by the ELR where an exterminating company was sued for fraud notwithstanding the contract which disclaimed liabilities. FOCUS IS THUS ON NEGLIGENCE AS TO THIRD PARTIES, OR WHERE INJURY RESULTS, FROM BREACH

Footnotes

[FN1]. William David Flatt, Note, *The Expanding Liability of Design Professionals*, 20 Mem. St. U. L. Rev. 611 (1990).

[FN2]. Richard O. Gamble, II, *How to Reduce Professional Liability for Engineers and Architects I* (1987).

[FN3]. *Id.* at 74.

[FN4]. *Id.*

[FN5]. Flatt, *supra* note 1, at 612.

[FN6]. *The American Heritage Dictionary of the English Language* 96 (3d ed. 1992).

[FN7]. *Id.* at 610.

[FN8]. See 4 Stuart M. Speiser Et Al., *The American Law of Torts* 813 & n.84 (1987) (citing *National Housing Indus., Inc. v. E.L. Jones Dev. Co.*, 576 P.2d 1374 (Ariz. Ct. App. 1978); *Caldwell v. Bechtel, Inc.*, 631 F.2d 989 (D.C. Cir. 1980)). See also Richard K. Allen, *Liability of the A/E to Third Parties*, Part 2, 38 *The Construction Specifier* 17 (1985); George M. Bell, *Professional Negligence of Architects and Engineers*, 12 *Vand. L. Rev.* 711 (1959); Douglas W. Eaton, Note, *The Ohio Supreme Court Takes a Step Back in Time: The Use of Privity to Shield Architects From Liability for Negligence*, 20 *Cap. U. L. Rev.* 1017 (1991); Jay A. Felli, Comment, *The Elements of Ohio's Liability Provisions for Contemporary Design - Build Architects - An Unwillingness to Expand the Plan*, 17 *U. Dayton L. Rev.* 109 (1991); Richard Gamble, *How to Reduce Professional Liability for Engineers and Architects* (1987); *How to Protect Yourself*

From *Lawsuits*, 59 *Better Roads* 31 (1989); Michael C. Loulakis, et al., *Negligent Supervision: How the Engineer is Liable*, 1982 *Civ. Engineering ASCE* 20; Paul M. Lurie & Barry D. Weiss, *Computer Assisted Mistakes*, 5 *Civ. Engineering* 78 (1989); John C. Peck & Wyatt Hoch, *Liability and the Standards of Care*, 58 *Civ. Engineering* 70 (1988); John C. Peck & Wyatt A. Hoch, *Liability of Engineers for Structural Design Errors: State of the Art Considerations in Defining the Standard of Care*, 30 *Vill. L. Rev.* 403 (1985); Karen S. Precella, *Architect Liability: Should an Architect's Status Create a Duty to Protect Construction Workers From Job-Site Hazards?* 11 *AUG Construction Law* 11 (1991); George L. Reed, *Coping With Litigation*, 55 *Civ. Engineering* 60 (1985); George L. Reed, *Improve Inspections and Reviews to Reduce Liability*, 1988 *ITE J.* 33 (1988); Bruce H. Schoumacher, *Update: Immunity of Federal Government Contractors*, 4 *Consulting/Specifying Engineer* 29 (1988); Robert E. Vansant, *Liability of Professional Engineers*, 1984 *APWA Rep.* 18; Mary Yuen, *Note, Absent Privity of Contract, Contractors May Not Recover Economic Damages Caused by an Architect's Negligence: Floor Craft Floor Covering, Inc. v. Parma Community Gen. Hosp. Ass'n*, 560 *N.E.2d* 206 (Ohio 1990), 60 *U. Cin. L. Rev.* 565 (1991).

[FN9]. *Donnelly Constr. Co. v. Oberg/Hunt/Gilleland*, 677 *P.2d* 1292, 1295 (Ariz. 1984).

[FN10]. See generally W. Page Keeton Et Al., *Prosser and Keeton on the Law of Torts* ss 28-40, 53-64 (5th ed. 1984 & Supp. 1988).

[FN11]. See, e.g., *Parkway Co. v. Woodruff, Presley, Mickelson & Klein, Inc.* 857 *S.W.2d* 903 (Tex. Ct. App. 1993), modified 901 *S.W.2d* 434 (Tex. 1995). After being sued by purchasers of a home, the defendant-developer in Parkway brought a third party claim against the engineers for

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