High Court on Pure Economic Loss - Unanimous in its Differences

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IF SOMEONE NEGLIGENTLY DOES something or fails to do something and this causes reasonably foreseeable commercial damage to someone else, what are that person's legal liabilities to the party which suffered commercial loss?

If the damage includes *physical* damage to a person or property, the answer is fairly clear-cut. The courts are likely to find that the negligent party has a duty of care to the person suffering the damage, has breached this duty and must pay compensation not only for the physical damage but also for the commercial loss.

But if there is no physical damage, and the loss is *purely* commercial (or *economic*, to adopt the language of the courts) it's a different story. And, as the High Court's August 12 1999 decision in *Frank Perre and others v Apand Pty Ltd* makes clear, if you ask any seven High Court judges, you'll get seven different answers!

This case had nothing to do with the construction industry. It was about potatoes which had a disease called bacterial wilt. But it involved the same legal issues as a series of cases on purely economic damage that have directly concerned the construction industry. One of those cases was *Bryan v Maloney*, in which a negligent house builder was held liable for the economic losses of the third owner of a house when inadequacies in its footings became apparent many years later.

Apand, a potato crisp manufacturer, supplied diseased potato seeds to South Australian growers who normally exported much of their crop to Western Australia. When the disease broke out, all potato producers within 20 km of the outbreak were automatically prohibited by WA quarantine regulations from exporting to WA for five years. Even though most of the potatoes were disease-free and had therefore suffered no physical damage, the commercial damage was catastrophic.

The SA growers who suffered physical damage when the disease was introduced to their farms won their negligence actions against Apand. The others lost, and appealed. In the High Court they won. The court decided Apand had owed the growers and processors a duty of care not to inflict purely economic damage.

The problem is, each of the judges used different reasons and spelt out quite different legal principles.

THE COMMON GROUND . . .

However, there was *some* common ground.

Reasonable foreseeability of the damage is necessary for a negligence claim to succeed, but for purely economic damage it is not sufficient to give rise to a duty of care. This was hardly surprising. One of the basics of a market economy such as Australia's, long recognized by the courts, is that one participant's commercial gain may be at another's loss.

Equally, however, there is no absolute rule precluding recovery for negligence which causes purely economic damage. Again, this has been clear in Australia since 1976. In deciding what else is required, on top of *foreseeability*, the courts are inevitably making value or policy judgments, weighing up competing factors and interests. Almost all the judges candidly acknowledged this, even though they differed on the principles to be followed and the policies that ought to be applied.

They were united, however, in rejecting a broad test of policy without either some type of guiding framework or principles or, more narrowly, the guidance of analogous cases from the past.

A duty of care not to inflict economic damage may be owed not merely to known individuals but also to a *class of people* who

need not be able to be precisely identified at all times, provided they are readily able to be ascertained and the class is thus not *indeterminate*. This class of potential claimants may be large. The principle is to *protect the defendant against indeterminate liability, not numerous plaintiffs.*

Otherwise, this area of law is a mess (not the High Court's words!), without much agreement on guiding principles for deciding policy questions.

. . . AND THE SHIPS PASSING IN THE NIGHT

Now for the differences.

In the past, one approach to the extra ingredients required before a duty of care arises has been a requirement of *proximity* or *closeness* in the relationship of the plaintiff and defendant. This approach was endorsed by four of the seven judges, although one added a separate *fairness* test and another a *special relationship*, a *large measure of control* and *special circumstances*. It was rejected by the other three judges as *lacking definition* and *indeterminate*.

A second approach has been to ask whether the facts fit an established category of cases where liability has been found in the past, such as negligent misstatement. One judge adopted this approach and argued for a new category, the destruction or impairment of a legal right by a person in a position to control the exercise or enjoyment of this right. Another looked for categories, but only as one of a series of possible tests, and expressly rejected the proposed new category. Three judges rejected the categories approach overall, and two remained neutral.

A third approach, developing in England, involves three stages: a *reasonable foreseeability* test; a *proximity* test; and, if both are satisfied, a *policy* test – whether it is *fair*, *just* and *reasonable* to impose the duty of care. This approach was adopted by only one judge. It was expressly rejected by two, one of whom commented that ideas of justice and morality should be invoked only as a criteria of last resort, and was impliedly rejected by the other four, although three addressed exactly the same policy issues without resorting to a separate policy test.

A fourth approach has been to eschew the search for new principles and rely on incremental development of the law, court case by court case. This was advocated by one judge who said the reasoning and policies of previous cases should be treated, where possible, as legal rules to be applied. The others accepted that the law would develop incrementally, but said earlier cases simply pointed to the factors to be considered.

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The advocate of this approach said the cases showed that even if the facts did not fall within an established category of liability, if economic damage had been reasonably foreseeable there *might* be a duty of care, depending on:

► How vulnerable the plaintiff had been to losses caused by the defendant's conduct, and whether the defendant had actually known (or ought of have known) of the risk and its magnitude.

Indicators of a plaintiff's vulnerability included control or an assumption of responsibility by the defendant and reliance by the plaintiff, but insurance was irrelevant.

► Even if the defendant actually knew of the risk, whether the defendant was legitimately protecting or pursuing his or her social or business interests.

Interestingly, this judge said not all unlawful conduct would be illegitimate. For example, it would be curious if misleading and deceptive conduct or restrictive trade practices in breach of the *Trade Practices Act* automatically meant that a defendant

owed a duty of care to all those he or she knew would be affected by the breach.

▶ Whether the liability would be confined to a readily ascertainable class of plaintiffs.

▶ Other factors such as economic efficiency in risk allocations.

The judges differed about the class of plaintiffs that could be readily ascertained. Several commented that liability should not extend to (for example) local storekeepers whose business declined, even though these impacts were clearly foreseeable.

Seven judges were prepared to include potato processors affected by the WA quarantine law, along with growers within the affected 20 km zone. But one excluded the affected potato processors because they might have been located outside the zone, and another also excluded all potato growers within the zone who had sold their potatoes to an exporting grower rather than export them directly themselves.

INTERPRETATION

So in the end, the High Court reached different conclusions in applying one of the few legal principles upon which the seven judges agreed – and reached fairly similar conclusions in applying quite different legal principles upon which they could only agree to disagree.

About all that can be said with certainty is that the class of plaintiffs in any particular case may be quite extensive, provided it is ascertainable, and that liability for purely economic damage will depend on the factors considered by almost all the judges within their different theoretical frameworks: the *closeness of the relationship*; the defendant's *actual and constructed knowledge* of the risk and the potential plaintiffs; the *extent of potential interference* with legitimate social or business interests; and the *vulnerability of the plaintiffs*.

So the potential extension of *economic damage only* negligence liabilities such as those found in *Bryan v Maloney* to the commercial environment (e.g. to a subsequent business purchaser of a building) will not *necessarily* be ruled out simply because only commercial premises and players are involved. It will, as they say, all depend on the facts. ■

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