The wreck of the

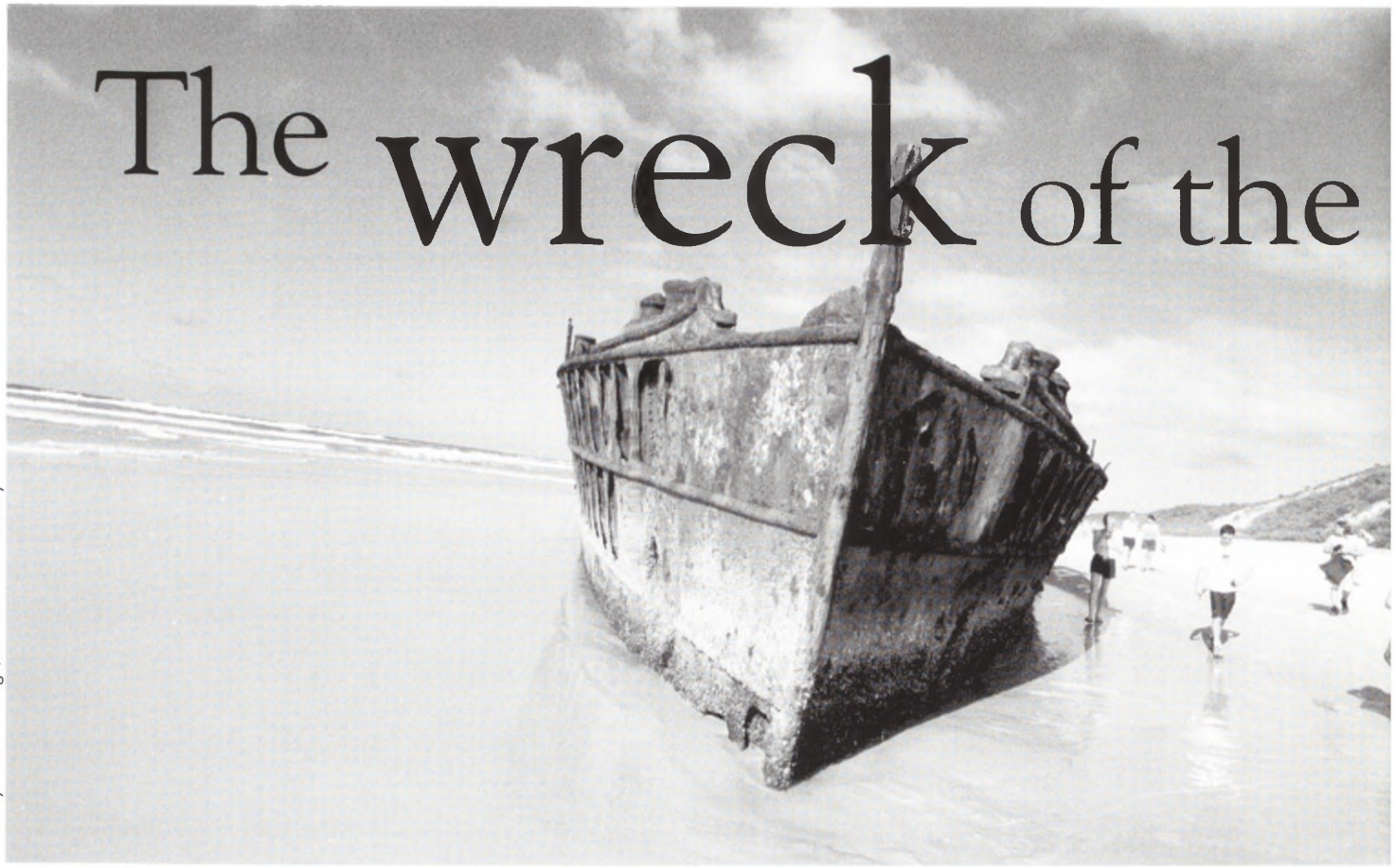

Photo by Robert Rough, Fairfax Photo Library.

In 1976, the High Court accepted that there were circumstances in which the law recognised a duty of care which would permit recovery of pure economic loss in tort: *Caltex Oil (Australia) Pty Ltd v The Dredge 'Willemstad'* (1976) 136 CLR 529.

To understand what then happened to the good ship *Willemstad* one must go back in time to Lord Atkin's celebrated statement in *Donoghue v Stevenson* [1932] AC 562 at 580:

"...rules of law arise which limit the range of complainants and the extent of their remedy. The rule that you are to love your neighbour becomes in law, you must not injure your neighbour; and the lawyer's question, Who is my neighbour? receives a restricted reply. You must take reasonable care to avoid acts or omissions which you can reasonably foresee would be likely to injure your neighbour. Who, then, in law is my neighbour? The answer seems to be - persons who are so closely and directly affected by my act that I ought reasonably to have them in contemplation as being so affected when I am directing my mind to the acts or omissions which are called in question."

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At 599 Lord Atkin described the effect of his approach:

"a manufacturer of products, which he sells in such a form as to show that he intends them to reach the ultimate consumer in the form in which they left him with no reasonable possibility of intermediate examination, and with the knowledge that the absence of reasonable care in the preparation or putting up of the products will result in an injury to the consumer's life or property, owes a duty to the consumer to take that reasonable care."

But, as Wilcox J said in *McMullin v ICI* (1997) 72 FCR 1 'this is the beginning of the modern story, not the end'.

The difficulty for lawyers practising in the area of economic loss claims is that this statement has been more honoured in the breach than in the adherence.

The main reason is that English judges immediately and effectively reverted back to a time before 'the beginning' and confined the dictum to "negligence which results in danger to life, danger to limb, or danger to health" (*Old Gate Estates Ltd v Toplis* [1939] 3 All ER 209 at 217).

The majority of the English Court of Appeal in *Candler v Crane, Christmas & Co* (1951) 2 KB 164 at 179 accepted that damage to tangible property could also attract Lord Atkin's neighbour test; but it said that it had "never been applied where the damage complained of was not physical" (at 184).

Yet one year before *Donoghue v Stevenson*, in the US Supreme Court, Chief Justice Cardozo in *Ultramares Corporation v Touche* (1931) 174 NE 441 at 444, without so restricting the damage, had cautioned against the imposition of liability in tort "in an indeterminate amount for an indeterminate time to an indeterminate class."

Lord Atkin did not take up this caution yet many others since, whilst proclaiming their loyalty to the neighbourhood principle, have heard the cock crow thrice.

The quirkiness of our common law system, as so clearly evidenced by the wilful blindness of those who sought to defend the landlord's coffers by maintaining that somehow *Cavalier v Pope* survived *Donoghue v Stevenson*, allowed a similar digression, in claims for pure economic loss, from the basic purpose of the common law, which is to do justice in accordance with community standards as they exist at the time.

Even if one accepted that Lord Atkin had no knowledge of what was happening in the other highest court in

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Willemstad found in a potato field

the English speaking world at the time that he chose not to impose a similar caution to that of Cardozo, CJ, the *Ultramares* dictum did not prohibit the extension of the duty of care to avoid causing pure economic loss. It ought always have been a matter for the Court to decide on the facts of the case before it whether the duty exists.

As Denning LJ said in *Candler* (at 179):

"I can understand that in some cases of financial loss there may not be a sufficiently proximate relationship to give rise to a duty of care; but, if once the duty exists, I cannot think that liability depends on the nature of the damage."

A generation after *Donoghue v Stevenson* the law recovered some lost ground with the decision of the House of Lords in *Hedley Byrne Co Ltd v Heller & Partners Ltd* [1964] AC 465, allowing recovery for economic loss sustained as a result of reliance on a negligent misstatement.

However, as per Kirby J in the case under review:

'Since Hedley Byrne, in all jurisdictions of the common law, judges have conducted a search for an "intelligible principle" which could replace the discredited exclusionary rule.'

The *Caltex* fact situation called for a natural application of the neighbourhood principle in the Australian community in 1976 but by then it was clear to the Court that there was this general exclusionary rule that the law did not allow recovery of pure economic loss.

Thus, the Court, including Mason J, felt constrained to find an exception to the alleged rule rather than apply the frank wisdom of Lord Atkin.

Stephen J stated that any duty to avoid any reasonably foreseeable financial harm needed to be constrained by "some intelligible limits to keep the law of negligence within the bounds of common sense and practicality" (at 573).

Despite the clear reasoning of the majority in the *Caltex* case, judges at first instance and lower appellate courts saw even this decision as a bolder step than they were prepared to take and tended to focus more on the constraints than the fundamental duty and the dredge sank back into the mud of Botany Bay.

A decade later, in *Sutherland Shire Council v Heyman* (1985) 59 ALJR 564 at 581 Mason J sought to raise the wreck from its watery grave when he said:

"The proposition that, in general, damages are not recoverable for economic loss unless it is consequential upon injury to the plaintiff's personal property is by no means absolute or inflexible; it is a reflection of the law's concern about endless indeterminate liability. In the absence of any such concern in a particular class of case there is no necessity to give effect to the proposition.....In this case it matters not whether the damage sustained by the respondents is characterised as being economic loss or physical damage. It is how the affair stands, viewed from the appellant's (defendant's) perspective, that is important in relation to a duty of care. To deny the existence of a duty of care solely by reason of the legal characterisation of the respondents' loss as economic- because the structure was flawed before they acquired property in it - is to ignore the significance of other circumstances in which the loss was sustained, circumstances which the appellant could reasonably foresee."

But again, his Honour's lead was not taken up with vigour by those occupying the lower benches and the hull dropped back into the mire.

Justice Burchett dived down to view the wreck in 1994 in *Alec Finlayson Pty. Ltd. v Armidale City Council & anor* (1994) FCR 378, where he said, at para. 82:

"The view expressed by Mason J (in ▶

Hawkins v Clayton *at 466) is pertinent to the present case. The applicant's loss reflects, in large measure, the cost of remediation aimed at the removal of the hazards of toxicity and carcinogenicity to persons and particularly children who might live upon or in the vicinity of lots in the various subdivisions. The validity of taking account of this aspect of the loss suffered by the applicant would not be affected by an acceptance of the conclusion of Deane J that the losses should correctly be characterized as economic. Like a finding of causation in the eye of the law (cf.* March v E and M.H. Stramare Pty. Limited *(1991) 171 CLR 506), the assignment by the law of a duty of care to a party occupying a particular position should reflect a common sense evaluation of the situation, in the light of human experience, rather than a nice assessment of how a legal taxonomy might categorise the plaintiff's loss. In* Sutherland Shire Council v Heyman, *all three judges of the majority lent some support to what Deane J...called 'a clear trend of recent authority' recognising that the general principles of negligence normally extend to cases involving mere economic loss, although in some particular situations they may not do so. A widening of the categories of cases in which claims for pure economic loss may be sustained is also supported by the more recent decision of the Supreme Court of Canada in* Canadian National Railway Co. v Norsk Pacific Steamship Co. Ltd. *(1992) 91 DLR [4th] 289."*

One year later and by this time holding a position akin to Harbour Master, Mason CJ in *Bryan v Maloney* (1995) ATR 81-320 at 62,099 gathered a salvage crew and serious work began on resurrecting the application of a duty of care to situations of pure economic loss other than misstatement.

The majority held that where a relationship between plaintiff and defendant is marked by the kind of assumption of responsibility and known reliance commonly present in the circumstances of that case there was a relationship of proximity which existed with respect to pure economic loss: see *Bryan v Maloney* per Mason CJ, Deane and Gaudron JJ at 62,101.

The issue of persuasive policy reasons for supporting the recognition of a relationship between a plaintiff and a defendant with respect to a particular kind of economic loss suffered was important to the majority. They included the consideration that, by virtue of superior knowledge, skill and experience, it was likely that a defendant would be better qualified and positioned to avoid, evaluate and guard against the financial risk posed by the act or omission: see *Bryan v Maloney* , at 62,101 and *Finlayson's* case at para 66.

At least the common law was left with a clear statement that the fact that the loss suffered is pure economic loss is clearly, of itself, not sufficient to disallow any duty of care.

There evolved other 'intelligible limits' as suggested by Stephen J in *Caltex*, whereby if the facts of a case fell within an existing category of assumption of responsibility and there was, initially, specific reliance/dependence as in *Hedley Byrne and Mutual Life & Citizens Assurance Co. Ltd. v Evatt* (1968) 122 CLR 556; (1970) 122 CLR 628; (1971) AC 793 but, later, general reliance/dependence as in *Bryan v Maloney* or *Hill v Van Erp* (1997) 142 ALR 687, recovery of damages was available.

Secondly, the Court, in circumstances where there was no existing category, would still embark on the determination of the issue of whether the facts of the case were such as would allow the extension of the duty of care either by the incremental approach or the application of the law of negligence to a completely novel situation.

The learned authors R.P. Balkin and J.L.R. Davis in *Law of Torts* (2nd Ed.) at 428 offered some guidance:

"...it can scarcely be doubted that the same principles [as in the Caltex case] would apply if there had been a small and ascertainable group likely to suffer that [economic] loss. It would make little sense, to take the example of the Caltex case, to say that if two or three oil companies had each used the pipeline, none of them could have recovered the costs flowing from its being damaged, whereas Caltex could recover, because it was the sole owner. The High Court, it may be observed, drew a distinction between an individual and the members of an unascertained class; it is at least plausible that the members of an ascertained class, if that class is suitably restricted in size, would be treated in the same way as an individual."

Because of the failure to apply the neighbourhood principle to situations of pure economic loss from the early 1930's, it had been necessary in more recent times for the High Court to go through both mental and linguistic gymnastics to be able to deliver justice. As such there had been an increasing reliance upon, and adoption of, the reasoning of Gaudron J as to control and more recently legal rights as being the determinant issues in such cases.

As with *Northern Sandblasting Pty Ltd v Harris* (1997) 71 ALJR 1428 the High Court, when recently faced with the perfect opportunity to lay the matter to rest once and for all, again fell short of a definitive statement bringing claims for pure economic loss back into the true neighbourhood fold. The illegitimate offspring remains out in the cold and the convoluted reasoning required in such an environment to deliver justice to meritorious (on the neighbourhood principle) claims continues.

In *Perre v Apand Pty Ltd* (1999) ATR 81-516 the High Court was faced with a claim by potato farmers and processors for damages for pure economic loss arising out of a refusal by Western Australian authorities to allow their produce into the State because of fears that such produce might be contaminated with a bacterial wilt.

At first instance, one of the potato farmers, Sparnon, had succeeded in establishing that a duty of care was owed to him by his supplier of tubers who supplied contaminated goods. None of his neighbours had purchased the contaminated tubers but they became guilty by association because of the risk of inter-farm contamination and suffered similar losses through denial of access to the market. Justice von Doussa of the Federal Court decided to follow the reasoning of the Full Court of the South Australian Supreme Court in *Seas Sapfor Forests Pty Ltd v Electricity Trust of South Australia* (Doyle CJ, Bollen and Nyland JJ, 9 August 1996, not reported) and declined the neighbours relief on the basis of insufficient proximity.

The same reasoning was adopted soon afterwards by Wilcox J in *McMullin v ICI* in denying cattle-producing neighbours of cotton farms compensation for being precluded from access to markets by a similar guilty association even though no contamination of their cattle was established. His Honour limited recovery to those producers who were able to prove that their property (cattle) was damaged (contaminated) and stated that the contaminated cattle, being the connecting link, provided the necessary proximity. He said:

"To accede to the applicants' submission in respect of the sixth and seventh category claimants would be to ignore the "general rule" stated by Gibbs J in Caltex, that "damages are not recoverable for economic loss which is not consequential upon injury to the plaintiff's person or property". Though the exceptions have expanded, the rule remains."

Unlike the cattle producers, the potato growers sought the intervention of the Full Court of the Federal Court but their Honours O'Loughlin, Branson and Mansfield JJ were unanimous in declining to overturn von Doussa J's findings. The potato growers were granted leave to appeal to the High Court.

In the High Court, all seven judges upheld the appeal and all were of the opinion that there was a general rule that damages for pure economic loss were not recoverable, however, there the unanimity stopped despite Kirby J's motherhood statement in repeating the unsatisfied mantra of all High Court watchers in the decades since Sir Owen Dixon led a unified bench:

"This appeal affords this Court an opportunity to clarify the law. Plainly it is an area of the law which calls out for such treatment. Only a measure of reconceptualisation will provide an enduring foundation for the application of legal principles to this and future cases in the place of the present disorder and confusion."

Unfortunately, the opportunity was not seized by his brethren nor was he able to convince them that his view of the reconceptualisation was the one they ought follow.

Gleeson CJ saw *"knowledge (actual, or that which a reasonable person would have) of an individual, or an ascertainable class of persons, who is or are reliant, and therefore vulnerable, is a significant factor in establishing a duty of care."*

On the facts of this case, the Chief Justice found *"actual foresight (on the part of the supplier) of the likelihood of harm, and knowledge of an ascertainable class of vulnerable persons."*

And later:

"Furthermore, the combination of circumstances involving the use and ownership or enjoyment of land, the physical propinquity of such land to the Sparnons' land, the known vulnerability of people in the position of the appellants, and the control exercised by the respondent over the relevant activity on the Sparnons' land, is unlikely to apply to an extent sufficient to warrant an apprehension of indeterminate liability."

Justice Gaudron sought refuge in her own 'control' doctrine supported by the 'legal rights' addition which had arisen in *Hill v Van Erp* and stated:

"In my view, where a person knows or ought to know that his or her acts or omissions may cause the loss or impairment of legal rights possessed, enjoyed or exercised by another, whether as an individual or as a member of a class, and that that latter person is in no position to protect his or her own interests, there is a relationship such that the law should impose a duty of care on the former to take reasonable steps to avoid a foreseeable risk of economic loss resulting from the loss or impairment of those rights."

The Court's second most senior judge took up the salvage of the dredge Willemstad and the poor rusted old girl finally saw the full light of day for the first time in 23 years when his Honour stated:

"...the decision in Caltex was correct. Although the facts of the present case are very different from those present in Caltex, the reasons (with some modification) that led this Court in that case to hold that the defendant owed a duty to the plaintiff to protect it from economic loss, apply here. The losses suffered by the Perres were a reasonably foreseeable consequence of Apand's conduct in supplying the diseased seed; the Perres were members of a class whose members, whether numerous or not, were ascertainable by Apand; the Perres' business was vulnerably exposed to Apand's conduct because the Perres were not in a position to protect themselves against the effects of Apand's negligence apart from insurance (which is not a relevant factor); imposing the duty on Apand does not expose it to indeterminate liability although its liability may be large; imposing the duty does not unreasonably interfere with Apand's commercial freedom because it was already under a duty to the Sparnons to take reasonable care; and Apand knew of the risk to potato growers and the consequences of that risk occurring."

However his Honour was not willing to return to pure Atkinsian thinking:

"Denial of recovery for pure economic loss remains the rule, but, since Hedley Byrne & Co Ltd v Heller & Partners Ltd *was decided in 1963, many exceptions to the rule have been recognised."*

Having discounted proximity and legal rights as the mechanisms by which the Courts ought avoid the so-called general rule, his Honour then aligned his reasoning with that of the Chief Justice and saw that what was:

"likely to be decisive, and always of relevance, in determining whether a duty of care is owed is the answer to the question, "How vulnerable was the plaintiff to incurring loss by reason of the defendant's conduct?" So also is the actual knowledge of the defendant concerning that risk and its magnitude. If no question of indeterminate liability is present and the defendant, having no legitimate interest to pursue, is aware that his or her conduct will cause economic loss to persons who are not easily able to protect themselves against that loss, it seems to accord with current community standards in most, if not all, cases to require the defendant to have the interests of those persons in mind before he or she embarks on that conduct."

His Honour also lowered the importance of assumption of responsibility and reliance to merely indicators

of this new disclosed (his Honour having felt it had been there unexpressed for many years) vulnerability principle.

Justice Gummow, with whose reasoning the Chief Justice stated he agreed despite the fact that Gummow J placed no reliance on vulnerability, took an active role in the Willemstad's rebirth and opined that, having rejected the incremental approach and the existing category approach, he preferred:

"the approach taken by Stephen J in Caltex Oil. *His Honour isolated a number of 'salient features' which combined to constitute a sufficiently close relationship to give rise to a duty of care owed to* Caltex *for breach of which it might recover its purely economic loss. In* Hill v Van Erp *and* Pyrenees Shire Council v Day *(1998) 192 CLR 330 at 389, I favoured a similar approach, with allowance for the operation of appropriate 'control mechanisms'."*

Kirby J remained with the three-fold foreseeability, proximity and policy approach he had reasoned with in *Pyrennees Shire Council*, and even found these three tests in the Caltex judgment, thus lending credence to his approach.

Justice Hayne travelled into somewhat uncharted territory to reason that the issue of liability for pure economic loss was to be answered:

"... by asking what would have been the position if the conduct had been engaged in deliberately."

His Honour found no disciples to this test amongst his colleagues on the bench.

Justice Callinin preferred the ambit approach and required there to be factors which, in combination:

"..establish a sufficient degree of proximity, foreseeability, a special relationship, determinacy of a relatively small class, a large measure of control on the part of the respondent, and special circumstances justifying the compensation of the appellants for their losses"

but also willingly helped his brother McHugh J haul the dredge from its prior resting place.

Their Honours, by majority, have breathed new life into the area of pure economic loss claims but it remains the case that *'liability depends on the nature of the damage'* irrespective of the fact that such a distinction is illogical and contrary to the dicta which started it all.

One wonders how long the dichotomy based on type of damage will last bearing in mind that other archaic distinctions such as pertained to occupiers' liability and landlords' liability have ceased to exist, and significant inroads have been made into the protection from liability previously enjoyed by public authorities for omissions.

In fact, one could even suggest that if the three foreseeabilities of identity, occurrence and type of damage are satisfied, the onus ought to be on the defendant to show that in a particular situation the duty ought not to extend the recovery of pure economic loss.

Sounds like something someone might have said back in 1932! PL