

The Appellate Strategist

INSIGHTS ON APPELLATE ISSUES, TRIAL CONSULTATIONS, AND EVALUATING APPEALS

Extending the Economic Loss Rule to Service Contracts in Arizona

June 13, 2011 by [Kirk Jenkins](#)

From time to time, I've reported on important new decisions from around the country on the scope of the economic loss rule, see [here](#), and [here](#), and [here](#). Last month, the Arizona Court of Appeals gave the defense bar an important new precedent, extending the economic loss rule to service contracts.

First, to review: economic losses are frustrated commercial expectations: "it wasn't worth what I paid," or "it broke," or "I didn't make as much money as I expected." The economic loss rule, simply stated, holds that where a plaintiff has suffered nothing but economic losses, tort claims are barred, and he or she must sue, if at all, on the contract. Most states have found that the economic loss rule arises from a desire to promote contractual certainty by holding parties, in the vast majority of cases, to their bargain.

[Cook v. Orkin Exterminating Company](#) arose from a home construction project gone bad. When the plaintiffs occupied their new home, they discovered termite infestations. The general contractor referred the matter to its insurer, which hired the defendant. Plaintiffs entered into a contract with defendant to treat the termite problem. Unfortunately, it didn't work; in the end, the defendants treated the house eighteen times in eighteen years. Finally, the plaintiffs sued Orkin for breach of contract, breach of the implied covenant of good faith and fair dealing, breach of warranty, breach of fiduciary duty, negligence, negligent and intentional misrepresentation, and fraud. The trial court entered partial summary judgment, finding that defendant owed plaintiff no fiduciary duty, and that the economic loss rule barred plaintiffs' tort claims.

The central issue on appeal in *Cook* was whether the economic loss rule is applicable to service contracts. The court concluded that the underlying policy of upholding the parties' reasonable expectations, rooted in the contract, necessarily meant that the economic loss rule barred all of plaintiffs' tort claims.

Although a number of states have not yet taken the same step, the Court of Appeal's decision is certainly correct. Some have argued that the rule is solely intended to maintain the terms of the Uniform Commercial Code as an exclusive remedy where the Code applies, meaning that the rule should be limited to products liability. Nevertheless, many states have extended the economic loss rule to tort claims arising out of construction contracts. Given that construction contracts are to a considerable degree service contracts, both settled law and the policy underlying the economic loss rule should make the rule applicable to service contracts.

A quarter century ago, the Supreme Court recognized that if the trend towards introducing tort into everyday business disputes continued unabated, "contract law would drown in a sea of tort." The

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Arizona Court of Appeals has taken an important step towards redeeming the Supreme Court's long-ago promise.