How Ohio Law Addresses Economic Losses to Property Caused by Defective Products

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Ohio has had long history of addressing claims involving damages to property caused by a product and economic losses related to product defects. Those decisions have involved both the law of contracts and the law of torts. Since 1962, the law of contracts in Ohio concerning products has been found in the Uniform Commercial Code. The law of torts has been a matter of both common law and, since 1988, has partially been governed by R.C. 2307.71 – R.C.2307.80. This article will review how Ohio law has evolved over the years when a product causes property damage or economic losses and how the right to such a recovery depends on whether the plaintiff is a consumer or a commercial entity.

First, a bit of background on the development of the law regarding what we now call product liability law. Until 1958, a party in privity with a manufacturer could use express or implied warranties in the contract for sale of the product to sustain a successful claim for damages, but, for those consumers without privity with the manufacturer, their only remedy was a negligence claim.

For example, a house fire was allegedly caused in 1946 when an electric blanket manufactured by General Electric caught fire. The plaintiff brought two claims against GE, first a claim that it breached an implied warranty of merchantability and the implied warranty the blanket was reasonably fit for use as an article of bed clothing and the second, that the blanket was negligently manufactured and that GE failed to properly inspect or warn. The first claim was brought in hopes of avoiding contributory negligence from defeating their damage claim as a result of the fire.

The jury instructions set out contributory negligence as a defense to both the implied warranty claim and the negligence claim. The jury found the plaintiffs were negligent and returned a defense verdict. The Court of Appeals reversed the verdict on the breach of implied warranty and ordered a new trial, because they found the contributory negligence charge should not have applied to the breach of implied warranty claims.

That outcome was appealed to the Ohio Supreme Court in 1953, which decided the appeal in *Wood v. General Electric Co.*, 159 Ohio St. 273, 112 N.E.2d 273 (1953). The Supreme Court ruled in its second syllabus, that a "sub purchaser of an inherently dangerous article may recover from its manufacturer for negligence, in the making and furnishing of the article, causing harm to the sub purchaser or his property from a latent defect therein, no action may be maintained against a manufacturer for injury, based upon implied warranty of fitness of the article so furnished" (Syllabus 2). So as late as 1953, the only remedy for someone not in privity with the manufacturer was a negligence action with the risk, as was the case here, that contributory negligence would defeat the claim, even where the manufacturer was careless in its design or manufacture of a consumer product.

Five years later, in 1958, the Ohio Supreme Court became one of the earliest high courts to expand consumer remedies when it decided *Rogers v. Toni Home Permanent*

Co., 167 Ohio St. 244, 147 N.E.2d 612 (1958). In that case, the plaintiff bought a Toni Home Permanent set labeled "Very Gentle" and had her mother give her a permanent wave. However, what resulted was unsatisfactory because her hair was caused to "assume a cottonlike texture and become gummy; that her hair refused to dry; and that when the curlers furnished by defendant were attempted to be removed, her hair fell off to within one-half inch of her scalp." *Id.* at *1. Her complaint was based on theories of negligence, breach of an express warranty, and breach of an implied warranty. The latter two claims were dismissed by the trial court and, as was the practice before the adoption of the Civil Rules, she appealed those dismissals. While the appellate court reinstated the express warranty claim, it sustained the dismissal of the implied warranty claim. The decision to reinstate the express warranty claim was in conflict with a decision of another court of appeals, so the Supreme Court took up the issue.

The Supreme Court held that a manufacturer who makes representations which the consumer relies upon can be sued even though there was no direct contractual relationship between them. In other words, a consumer can sue a manufacturer for breach of an express warranty. The decision was grounded on the conclusion that such a breach was allowed as a matter of tort law and is not based on contract law, so that the lack of privity did not defeat the claim.

In 1965, the Supreme Court further expanded consumer rights in *Inglis v. American Motors Corp.*, 3 Ohio St. 2d 132, 209 N.E.2d 583 (1965), to allow consumers not in privity with the manufacturer to recover damages from the manufacturer for breach of an express warranty made in advertising that Rambler automobiles were trouble-free, economical in operation, and built and manufactured with high quality of workmanship and to recover damages for the diminution of value of an automobile attributable to the latent defects in the vehicle that breached those representations. The specific allegations were that "the cargo-area door was out of line, could not be opened, and continually squeaked and rattled; that the trimming about the door was torn; that the doors were out of line and squeaked and rattled, and that the door handles were loose; that the motor was extremely noisy, had been defectively cast and seeped substantial quantities of oil; that the steering gear was improperly set and creaked when turned; that the transmission emitted a groaning noise; that the brakes squeaked and grated; that the oil pump assembly was defective; that the front seat squeaked and rocked; and that loose parts inside of the car fell out from time to time endangering occupants of the car" *Id.* at 134. In other words, the purchaser of the car could recover for his or her economic loss caused by breach of an express warranty. However, because there was no privity between the buyer and the manufacturer, the breach of an implied warranty claim concerning quality and fitness of said automobile was denied, as was a negligence claim against the manufacturer by the buyer to recover the diminished value of the car for the manufacturer's alleged failure to discover or correct the defects in the car before sale.

In 1966 in *Lonzrick v. Republic Steel Corp.*, 6 Ohio St. 2d 227, 218 N.E.2d 185 (1966), the Ohio Supreme Court brought their prior decisions together and held that manufacturers were liable in tort when their products were defective because they were not fit for their ordinary purpose, even to those consumers who were not in privity with the manufacturer. No longer was a party not in privity with the manufacturer limited to pleading their damages were the result of a breach of an express warranty, now they could base their claim on a breach of the implied warranty that the product was safe for its ordinary use.

In 1975, the Supreme Court had to decide whether the cause of action for breach of implied warranty in tort was available in a case of property damages only. In *Iacono v. Anderson Concrete Corp.*, 42 Ohio St. 2d 88, 326 N.E.2d 267 (1975), the Supreme Court recognized the right of a homeowner who hired a cement contractor to install a drive way to recover damages from the concrete supplier from whom the homeowner's contractor purchased the concrete, after the concrete failed to withstand the winter because soft shale was included in the mix by the concrete company.

Whether a commercial entity could pursue a similar recovery was decided in *Chemtrol Adhesives v. Am. Mfrs. Mut. Ins. Co.,* 42 Ohio St. 3d 40, 537 N.E.2d 624 (1989). Chemtrol was in privity with the product manufacturer but the contract did not have remedy covering the damages to the industrial dryer it purchased from the manufacturer, or the costs to repair the dryer or for the increased production costs while the dryer as out of service. So it attempted to recover those

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damages from the manufacturer using the breach of an implied warranty in tort theory approved in *Iacono*.

Adopting the analysis of damages offered in *Mead Corp. v. Allendale Mut. Ins. Co.*, 465 F. Supp. 355, 363 (N.D. Ohio 1979), the Supreme Court recognized there are three types of damages which could be caused by a defective product; the first two were physical injury to persons or property. The third type of damage was economic loss, which had two components: 1) direct economic loss, the loss attributable to the decrease in value of the product because of the defect, and 2) indirect economic loss, the consequential damages caused by the defective product. Both of the latter economic loss claims existed in this case.

The court observed, "the determination of whether recovery in tort is available for damage to the defective product itself requires more than a simple labeling of that damage as 'property' or 'economic'" *Chemtrol Adhesives v. Am. Mfrs. Ins. Co., supra* at 44. It recognized "the law of negligence does not extend the manufacturer's duty so far as to protect the consumer's economic expectations, for such protection would arise not under the law but rather solely by agreement between the parties.... [T]he duty to provide a working arch dryer arose not under the law of negligence but rather under its contract with Chemtrol. Accordingly, it is the law of contracts, and not the law of negligence, to which Chemtrol must look for a remedy." *Id.* at 45.

The *Chemtrol* court concluded "a commercial buyer seeking recovery from the seller for economic losses resulting from damage to the defective product itself may maintain a contract action for breach of warranty under the Uniform Commercial Code; however, in the absence of injury to persons or damage to other property the commercial buyer may not recover for economic losses premised on tort theories of strict liability or negligence." Id. at paragraph 2 of the syllabus.

The court also noted a key distinction here from the prior cases. The plaintiffs in its prior decisions addressing economic loss, *Inglis* and *Iacono*, were not in privity with the manufacturing defendant. This was a critical difference of position, since the parties were not free to bargain over the quality of the goods.

So since 1989, while commercial buyers in privity with the manufacturer are limited to contractual remedies, what remedies are available for economic losses caused to commercial parties who are not in privity with the manufacturer?

The Ohio Supreme Court has not addressed this issue but in 1997, the Ninth District did address the issue in *Midwest Ford v. C.T. Taylor Co.*, 118 Ohio App. 3d 798, 694 N.E.2d 114 (9th Dist. 1997). Midwest had hired a general contractor to remodel the dealership and a flooring company subcontracted to install tile it would purchase from a flooring dealer (OBrien Cut Stone). The tile turned out to be defective and Midwest sued for the diminished value of the flooring and other damages as a result of the defects in the flooring.

The *Midwest* court reasoned that "Midwest has bargaining power at least equal to that of Contractor or O'Brien. Presumably, Midwest could have purchased warranty protection for the value of the floor from Contractor, but chose not to do so. Through this suit, Midwest seeks a better bargain than it struck. Permitting suit against O'Brien for strict liability for purely economic damages potentially shifts costs to O'Brien's other customers, be they non-commercial buyers or commercial buyers who manage contractual economic risks more conservatively than Midwest." *Id.* at 805.

However, in 2000, the Tenth District Court of Appeals addressed the same issue in a case involving a defective roof insulation supplied by a vendor to a subcontractor of the general contractor hired by the state to build a State Highway Department garage. The court in *Ohio Dep't of Admin. Servs. v. Robert P. Madison Int'l.*,138 Ohio App. 3d 388, 741 N.E.2d 551 (10th Dist. 2000), reviewed Midwest's reasoning but found no basis for distinguishing between so-called commercial and noncommercial buyers, thereby upholding the state's right to pursue the insulation manufacturer on a breach of an implied warranty in tort for economic damages resulting from the defect. That holding has been followed by the Fourth District Court of Appeals in *Caterpillar Fin. Servs. Corp. v. Harold Tatman & Son's, Enters.*, 2015-Ohio-4884, 50 N.E.3d 955 (4th Dist.), but by no other Ohio courts.

The other courts to consider whether a commercial plaintiff who is not in privity with the manufacturer can recover for economic loss have all rejected the claim. First, in

2003, the Third District Court of Appeals in *Norcold, Inc. v. Gateway Supply Co.*, 154 Ohio App.3d 594, 2003-Ohio-4252, 798 N.E. 2d 618, ¶35 (3d Dist.), for reasons similar to M*idwest Ford*, held that the "policies of product liability law as articulated by Ohio courts would not be served by extending a strict-liability cause of action to commercial plaintiffs" and declined to follow the reasoning in Department of Administrative Services decision.

The Sixth Circuit also addressed this issue and reasoned consistent with the *Midwest Ford* decision, rejecting the analysis in the Department of Administrative Services decision. In *HDM Flugservice GmbH v. Parker Hannifin Corp.*, 332 F.3d 1025 (6th Cir. 2003), the court concluded that allowing commercial buyers not in privity with the manufacturer to seek these remedies would undermine the provisions of the Uniform Commercial Code governing commercial transactions. "Among commercial parties, the U.C.C. provides a comprehensive scheme for parties to recover their economic losses. Permitting commercial parties to recover economic losses in tort would allow a purchaser to reach back up the production and distribution chain, thereby disrupting the risk allocations that have been worked out in the transactions comprising the chain. Moreover, policies underlying Ohio's strict liability are forcing manufacturers to internalize and redistribute the cost of injuries because they are in the best position to do so and relieving average consumers of the burden of proving negligence. These policies do not favor allowing commercial parties to recover their economic losses. [Citations omitted.] *Id*. at 1030.

In *Apostolos Group, Inc. v. BASF Constr. Chems., LLC*, 9th Dist. Summit No. 25415, 2011-Ohio-2238, the Ninth District reevaluated its Midwest decision in view of the Department of Administrative Services decision, but ended its analysis noting: "while the relative bargaining power of a commercial consumer will vary from case to case, the commercial consumer functions in a different capacity than the average customer. The fact that Thomarios did not have an opportunity to negotiate the warranty and product formulation of the Sonoguard does not mean that it was similarly situated as a member of the general public making a purchase for personal use. As a commercial consumer, Thomarios was presumably aware of the inherent risks involved in entering into a commercial endeavor. By making the decision to engage in the commercial endeavor of applying the deck coating at the Fowler apartments, Thomarios entered into an arrangement where Rasmussen could specify the type of deck coating used for the project. As the policies underlying the strict liability doctrine would not be served by allowing Thomarios to assert an implied warranty claim, the trial court did not err in following Midwest Ford." *Id.* at ¶16.

So at this point in the development of the law in Ohio remains clear consumers not in privity with the product manufacturer can recover in tort for economic losses caused by product defects, but there are two conflicting views concerning whether commercial parties have tort rights to recover economic losses caused by defects in the product against a manufacturer.

Having read this article you might ask "doesn't the Ohio Product Liability Act have something to say about these claims?"

The answer is not much. R.C. 2307.71(A)(13) says product liability claims include "claims for physical damage to property other than the product in question," and that is the only reference to non-personal injury claims defined as a "product liability claim." So claims for damage to the product, itself, and non-physical damages to other products, are outside the coverage of the product liability statutes in Ohio.

This point is made clear by these additional terms, defined in that same section of Revised Code. Part (A) (2) of the statute defines "economic loss" to mean "direct, incidental, or consequential pecuniary loss, including, but not limited to, damage to the product in question, and nonphysical damage to property other than that product. Harm is not "economic loss." As for the term "harm," it is defined in Part (A)(7) to mean "death, physical injury to person, serious emotional distress, or physical damage to property other than the product in question. Economic loss is not 'harm.'"

Finally, to make the intent more clear, R.C. 2307.72(C) states "Any recovery of compensatory damages for economic loss based on a claim that is asserted in a civil action, other than a product liability claim, is not subject to sections 2307.71 to 2307.79 of the Revised Code, but may occur under the common law of this state or other applicable sections of the Revised Code."

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Section 2307.79 of the Revised Code makes it clear that while economic loss is not recoverable under the product liability statutes, if compensatory damages are awarded for "harm" (as defined in R.C. 2307.71(A)(7) as, personal injuries and physical damage to property other than the product), the claimant may recover from the product manufacturer "compensatory damages for any economic loss that proximately resulted from the defective aspect of the product in question (R.C. 2307.79(A)) and "for any economic loss that proximately resulted from the negligence of that supplier or from the representation made by that supplier and the failure of the product in question to conform to that representation" (R.C. 2307.79(B)). So when compensatory damages are awarded for "harm," manufacturers and suppliers are also liable for "economic loss" as that term is defined in R.C.2307.71(A)(7).

At this time it is unclear whether this phrase, in R.C. 2307.79, "compensatory damages for any economic loss that proximately resulted from the defective aspect of the product in question" will allow a consumer or a commercial plaintiff suffering physical damages to other property as the result of a product defect to recover for "direct, incidental, or consequential pecuniary loss, including, but not limited to, damage to the product in question" by claiming those damages are among those defined in R.C.2307.71(A)(4) as economic loss and hence those damages become recoverable, by virtue of the language in R.C.2307.79. A commercial plaintiff, in privity with the manufacturer, but without a contractual right to those damages, may argue R.C. 2307.79 allows these damages to be recovered, as may a consumer or a commercial plaintiff not in privity with the manufacturer. There are no reported cases addressing how to apply R.C. 2307.79 as of this writing.

So while the rights of consumers to recover for economic losses when not in privity with the manufacturer is relatively settled in Ohio, the rights of commercial plaintiffs to recover against manufacturers for economic losses sustained as the result of a defective product remain unclear.

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