New Jersey Law Journal

VOL. CXCVI - NO.6 - INDEX 394 MAY 11, 2009 ESTABLISHED 1878

IN PRACTICE

PRODUCTS LIABILITY

The Economic Loss Doctrine:

A License to Sell Defective Building Products

BY JOHN RANDY SAWYER AND JOSEPH D. GUMINA

Underlying the entire complex of laws governing the construction and sale of residential property in New Jersey is a clear recognition that, "for most people, the purchase of a house will be the most important investment of a lifetime." *Gennari v. Weichert Co. Realtors*, 148 N.J. 582, 607 (1997). That understanding is reflected in 40 years of judicial and legislative advances against archaic common-law notions, such as *caveat emptor*, merger, and privity, that unfairly obstruct homebuyer remedies for material defects in construction. See, e.g. *McDonald v. Mianecki*, 79 N.J. 275, 294 (1979). Two recent Appellate Division decisions seem to move the law in a contrary direction. In *Marrone v. Greer & Polman Constr. Inc.,* 405 N.J.Super. 288 (App.Div. 2009), and *Dean v. Barrett Homes, Inc.,* 2009 WL 1025565 (App. Div. 2009), the Appellate Division upheld the application of the economic loss rule to shield manufacturers of defective building materials from liability to the purchasers of pre-owned houses that incorporate the materials and sustain physical damage as a result. The economic loss rule, as codified by the New Jersey Product Liability Act, limits the availability of tort remedies to plaintiffs who have suffered personal injury or "physical damage to property other than the product itself." N.J.S.A. 2A:58C-1(b)(2).

The critical issue addressed in *Dean* and *Marrone* is whether "the product itself," as applied to plaintiff homeowners, encompasses the entire house (disallowing tort claims for damage to other parts of the residence) or is limited to the defective building component supplied by the defendant manufacturer (allowing such claims). That question was previously answered in *DiIorio v. Structural Stone & Brick Co., Inc*., 368 N.J. Super. 134 (App. Div. 2004). In *DiIorio*, plaintiff homeowner filed suit against the manufacturer of defective stone siding that damaged the rest of the house in which it was integrated. The action was commenced outside the four-year statute of limitations of the U.C.C., but within the six-year statute applicable to claims for tortious injury to property. Concluding that "this [was] a product liability case[,]" the trial court permitted plaintiff to take advantage of the longer statute. On appeal, the manufacturer argued that the four-year statute should apply because "recovery of economic losses caused by goods that damage only the goods themselves are recoverable only in accordance with the comprehensive provisions of the U.C.C and not pursuant to theories of tort." In rejecting this argument, the court noted that the asserted damages were "not limited to the value of the stones themselves." Viewing the stones, not the damaged house, as the relevant "product," the court determined that plaintiff had sustained "other property" damage, recoverable in tort, outside the limitations of the U.C.C.

In *Marrone*, the Appellate Division revisited the issue of what constitutes "the product itself," as applied to pre-owned residential construction. Plaintiffs sued the manufacturer and distributor of an exterior siding product known as Exterior Insulation and Finish System (EIFS). They alleged that defects in the EIFS had allowed water to infiltrate and injure the underlying structure of their home. In dismissing plaintiffs' tort claims, the trial judge viewed the home as the relevant "product," concluding that plaintiffs had not alleged "personal injury or loss of personal property other than the damage

Sawyer is a shareholder and Gumina is an associate in the construction litigation group of Stark & Stark in Lawrenceville. Sawyer served as counsel for the plaintiffs in the Marrone *case.*

to the home itself." The Marrones argued on appeal that this ruling was inconsistent with *DiIorio.* The Appellate Division disagreed. Unlike the plaintiff in *DiIorio,* the Marrones "were not the original owners of the house. They bought the house. . . . from the original owners. . . who in turn had contracted for its construction[.]" The court determined that, as subsequent purchasers, plaintiffs could not circumvent the economic loss rule by "attempting to break the house down . . . into its component parts [.]" To conclude otherwise would, in the court's judgment, carry the realm of tort liability too far, potentially allowing "a buyer who purchased plaintiffs' house fifty years from now . . . [to] sue the [manufacturer and distributor of a defective building product] for water damage to the house." The policy of shielding manufacturers against "potentially unlimited liability" was deemed sufficient reason to foreclose plaintiffs' PLA remedies.

The combined result of *Marrone* and *DiIorio* is that, where a defective component causes damage to residential construction in which it is integrated, the manufacturer's liability in tort will run to the injured homeowner who has "contracted directly with a builder to construct a house[,]" but not to the subsequent purchaser who, though suffering the same injury, stands further "downstream in the chain of distribution." By limiting *DiIorio* in this manner, *Marrone* reanimates the notion of "privity" that was put to rest nearly a half century ago in *Henningsen v. Bloomfield Motors, Inc.,* 32 N.J. 358, 161 (1960).

The authors submit that *Marrone* was wrongly decided, as it conflicts with the prevailing rule that a manufacturer's liability to an end user of its product turns, not on privity, but on foreseeability. The key inquiry, which receives short shrift in *Marrone,* is whether a manufacturer who places a component in the stream of commerce for use in residential construction could reasonably envision anything but a class of end users that includes remote homebuyers. See N.J.S.A. 2A:58C-2. The answer to the court's concern of "potentially unlimited liability" is "not the judicial obstruction of a fairly grounded claim for redress[, but] a more sedulous application of traditional concepts of duty and proximate causation to the facts of each case." *People Exp. Airlines, Inc. v. Consolidated Rail Corp.,* 100 N.J. 246, 254 (1985).

On facts strikingly similar to *Marrone*, the Appellate Division in *Dean v. Barret Homes*, 2009 WL 1025565 (App. Div. 2009), again affirmed dismissal of PLA claims asserted by subsequent homeowners against the manufacturer of EIFS, where consequential damage had extended to other parts of the house. The panel issued two opinions: one by Judge Carchman delivering the judgment of the court; and the other by Judge Sabatino, concurring in the judgment but differing on the "critical issue" of what constitutes the relevant "product." Rejecting *DiIorio*'s analysis of that issue as *dicta*, Judge Carchman embraced the view of the *Marrone* court — that the house constitutes "the product itself" — and concluded that the damage to the home's underlying structure was not damage to "other property." This conclusion notwithstanding, *DiIorio*'s discussion of the economic loss rule cannot be relegated to the category of *dicta* where it was demonstrably on point with the issues presented by the appellants in that case. Indeed, Judge Sabatino, joined by Judge Simonelli, characterized Carchman's departure from *DiIorio* as "troublesome," and his resolution of the "critical issue" as inconsistent with "the dominant view of other states" that a defective component "incorporated into an improvement to realty does not lose its identity as a product[.]" Looking to the PLA, Sabatino expressed "considerable doubt that the Legislature intended to treat a single family house as a 'product'[.]" Despite their differences on the issue of what constitutes "the product itself," Carchman and Sabatino agreed that examination of unique transactional circumstances, particularly the relative ability of the parties in that case to avoid the loss asserted, weighed in favor of confining the Deans to their nontort remedies.

In the authors' view, Judge Carchman's analysis is problematic, both for its interpretation of the PLA and for its potential impact on homeowner protections. The PLA expressly excludes "seller[s] of real property" from the definition of "product seller." N.J.S.A. 2A:58C-8(1). This begs the question — if a seller of real property is not a "product seller" under the PLA, how then is a house, an improvement to the real property, considered "the product itself"? That view of the house would, under a literal reading of the PLA, confine homeowners to their warranty remedies whenever a defective component failed to spread devastation beyond the house itself. Consider defective wiring that starts a fire, resulting in nothing less (and nothing more) than the house's total destruction. Is this a mere disappointment of economic expectations for which the law affords no recourse outside of warranty? The ability of a homeowner to "recover down an unbroken chain of warranties to the original source of the defect is greatly impeded in construction cases by the high number of insolvencies, bankruptcies, and business failures in the industry." Cheezem, "Economic Loss in Construction Setting: Toward Appropriate Definition of 'Other Property,'" 12-*Apr Conslaw* 21, 23 (1992). Even where all parties remain subject to service of process, common experience in the "volatile world of contractors, subcontractors, and material suppliers" confirms the impracticality of supposing a sequence of breach of warranty claims, transferring loss from the afflicted homebuyer to the component manufacturer bearing ultimate responsibility. It seems unlikely the Legislature intended to shield manufacturers and deprive homeowners of a practical recourse under these circumstances.

At the end of the trail from *DiIorio* to *Marrone* and *Dean,* it is unclear whether a subsequent homebuyer has any remedy against a manufacturer of faulty building components that damage a pre-owned residence. *Marrone*'s conclusion that the PLA offers no remedy to such a homebuyer conflicts with the more permissive view of the concurring majority in *Dean*. Because Judge Carchman's endorsement of *Marrone* failed to attract a majority of the *Dean* panel, the line between *dictum* and rule of law was not crossed, and no new legal authority for that position was granted. The authors submit that *DiIorio*, as endorsed by Judge Sabatino, retains its persuasive force and, as to original homeowners, remains the settled law of New Jersey. ■